

AXCELIS TECHNOLOGIES INC
Form 10-K
March 11, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934

For the fiscal year ended December 31, 2018

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934

For the transition period from to

Commission file number 000-30941

AXCELIS TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

Delaware	34-1818596
(State or other jurisdiction	(IRS Employer Identification No.)
of incorporation or organization)	

108 Cherry Hill Drive

Beverly, Massachusetts 01915

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(Address of principal executive offices) (zip code)

(978) 787-4000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$.001 par value	The Nasdaq Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by checkmark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer	Non-accelerated filer	Smaller reporting company	Emerging growth company
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If an emerging growth company, indicate by check mark if registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

Aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2018: \$640,157,087

Number of shares outstanding of the registrant’s Common Stock, \$0.001 par value, as of March 4, 2019: 32,741,315

Documents incorporated by reference:

Portions of the definitive Proxy Statement for Axcelis Technologies, Inc.’s Annual Meeting of Stockholders to be held on May 14, 2019 are incorporated by reference into Part III of this Form 10-K.

PART I

Item 1. Business.

Overview of Our Business

Axcelis Technologies, Inc. (“Axcelis,” the “Company,” “we,” “us,” or “our”) designs, manufactures and services ion implantation and other processing equipment used in the fabrication of semiconductor chips. We believe that our Purion family of products offers the most innovative implanters available on the market today. We sell to leading semiconductor chip manufacturers worldwide. The ion implantation business represented 95.3% of our revenue in 2018, with the remaining 4.7% of revenue derived from other legacy processing systems. In addition to equipment, we provide extensive aftermarket lifecycle products and services, including used tools, spare parts, equipment upgrades, maintenance services and customer training.

Axcelis’ business commenced in 1978 and its current corporate entity was incorporated in Delaware in 1995. We are headquartered in Beverly, Massachusetts and maintain an internet site at www.axcelis.com. On or through our website, investors may access, free of charge, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. Our website and the information contained therein or connected thereto shall not be deemed to be incorporated into this Form 10-K.

Despite a significant slowdown in memory spending in the second half of 2018, revenue increased by nearly 8% over 2017, with systems revenue increasing by 6.7%, and revenues from Customer Support & Innovation (“CS&I”), our aftermarket business, increasing by nearly 10%. 2018 full year gross margin exceeded 40% and cash increased by 33% to \$178.0 million.

Our 2018 results were the product of hard work across the Company over prior years to expand the Purion install base to a large and diverse group of customers. We have focused on key markets in the mature process technology sector such as image sensor, power device and mature foundry and logic. We developed Purion product extensions specifically for these markets and becoming key partners with these customers. As a result, our fourth quarter 2018 revenues showed a split of 68% mature process technology and 32% memory, illustrating our expansion into the mature process technology sector, and the reduction in our dependence on memory customers. For the full year the mix was 54% mature process technology and 46% memory.

We continue to work diligently to ensure that manufacturing and operating expense levels remain well aligned to business conditions. We believe that the most fundamental interest of our stockholders is consistent, profitable, financial performance, which we expect to continue to deliver in 2019. Our performance is subject to risks and uncertainties discussed below under Item 1A Risk Factors.

Industry Overview

Semiconductor chips, also known as integrated circuits, are used in a continuously evolving range of consumer and industrial products, including for example, personal computers, mobile devices, automobiles, sensors and controllers for the “internet of things,” and data storage servers. Types of semiconductor chips include dynamic random-access memory (“DRAM”) and “negative and” (“NAND”) Flash memory; logic devices to process information; and “system on chip” devices (which have both logic and memory features). The increased number of devices providing information to and receiving information from the Internet, sometimes referred to as the “Connected World,” is increasing demand for chips. These chips are used in data input, such as image sensors, which are often manufactured using mature processing technologies, as well as for memory chips to support the storage of data, internet streaming and “cloud computing” data analytics.

Most semiconductor chips are built on silicon wafers of either 200mm (8 inches) or 300mm (12 inches) in diameter. Each semiconductor chip is made up of millions of tiny transistors or “switches” to control the functions of the

device. Transistors are created in the silicon wafer by introducing various precisely placed impurities into the silicon in specific patterns.

Semiconductor chip manufacturers own or manage wafer fabrication facilities (often referred to as “fabs”), which utilize many different types of equipment in the making of integrated circuits. Over 300 process steps utilizing over 50 different types of process tools are required to make a single device like a microprocessor. Semiconductor chip manufacturers seek device performance benefits through new products and technology enhancements and productivity improvements through increased throughput, equipment utilization and higher manufacturing yields. Capacity is added by increasing the amount of manufacturing equipment in existing fabrication facilities and by constructing new fabrication facilities.

We have different types of customers, which impacts timing of purchases and technology requirements. Some customers are integrated electronics manufacturers, making semiconductor chips for their own devices. These same companies may also act as foundries, manufacturing chips for other electronic manufacturers or chip design companies. Some customers only function as foundries. A few companies design and manufacture branded chips that are sold to device manufacturers. In addition, some customers have partnerships or joint ventures with two or more semiconductor chip manufacturers to share the technology development and capital investment. The timing of purchases by foundry customers will depend on their success in securing manufacturing contracts. Also, foundry customers will look for equipment that can deliver the broadest capabilities in order to be prepared to manufacture all chip types, while integrated electronics manufacturers may invest in processing equipment dedicated to a specific application they require for their products.

The semiconductor capital equipment industry is cyclical, as global chip production capacities successively exceed, then lag behind, global chip demand. When chip demand is high, and inventories low, chip manufacturers add capacity through capital equipment purchases. Given the difficulties of forecasting and calibrating chip demand and production capacity, the industry periodically experiences excess chip inventories and softening chip prices. Device manufacturers react with muted capital spending, lowering the demand for capital equipment. Changes in consumer and business demand for products in which chips are used also affect the industry. A successful semiconductor capital equipment manufacturer must not only provide some of the most technically complex products manufactured in the world but also must manage its business to thrive during low points in the cycle.

Axcelis' Strategy

Axcelis' 2019 strategic initiatives are:

- Continue to expand our Purion footprint within our existing customer base
- Penetrate Japanese and advanced foundry/logic markets with Purion
- Capitalize on successful market segmentation strategy by releasing new Purion product extensions focused on key market segments

- Drive Customer Support & Innovation revenues by delivering excellent customer service and innovative, high value products and services
- Deliver gross margins of 41% for full year 2019

We continue to invest in research and development to ensure our products meet the needs of our customers. We take pride in our scientists and engineers who are adding to our portfolio of patents and unpatented proprietary technology to ensure that our investment in technology leadership translates into unique product advantages. We strive for operational excellence by focusing on ways to lower our product, manufacturing and design costs and to improve our delivery times to our customers. Global Customer Teams and a focused account management structure maintain and strengthen our customer relationships and increase customer satisfaction. Finally, we endeavor to maintain a strong cash balance to ensure sufficient capital to fund business growth.

Ion Implantation Systems

Ion implantation is a principal step in the transistor formation cycle of the semiconductor chip manufacturing process. Ion implantation is also used to change the material characteristics of the silicon for reasons other than electrical doping, a process known as “material modification.” An ion implanter is a large, technically advanced system that injects dopants such as arsenic, boron or phosphorus into a wafer. These dopants are ionized and therefore have an electrical charge state. This electric charge state allows the dopants to be accelerated, focused and filtered with electric and magnetic fields. Ion implanters use these fields to create a beam of ions with a precisely defined energy level (ranging between several hundred and eight million electron volts) and with a precisely defined beam current level (ranging from microamps to milliamps). Certain areas of the silicon wafer are blocked off by a polymer material known as photoresist, which acts as a “stencil” to pattern devices so that the dopants will only enter the wafer where needed. Typical process flows require twenty implant steps, with the most advanced processes requiring thirty or more steps. Each implant step is characterized by four key parameters: dopant type, dose (amount of dopant), energy (depth into the silicon) and tilt/twist (angle of wafer relative to the ion beam).

In order to efficiently cover the wide range of implant steps, three different types of implanters have been developed, each targeted at a specific range of applications, primarily defined by dose and energy. The three traditional implanter types are referred to as high energy, medium current and high current:

- High energy implanters emerged to address the need for deeper implants with a high energy range and low dose.
- Medium current implanters are the original model of ion implanter, with mid to low range energy and dose capability.
- High current implanters were the second type of implanter to emerge, having low energy capability and high dose range.

The Purion Platform and Family of Ion Implanters

Axcelis offers a complete line of high energy, high current and medium current implanters for all application requirements. Our Purion flagship systems are all based on a common platform which enables a unique combination of implant purity, precision and productivity. Combining a state of the art single wafer end station, with advanced spot beam architectures (that ensures all points across the wafer see the same beam condition at the same beam angle), Purion products enable exceptional process control to optimize device performance and yield, at high productivity.

High Energy Implant. Our Purion XE high energy system combines Axcelis' production proven RF Linac high energy, spot beam technology with the Purion platform wafer handling system. Axcelis is a market leader in high energy ion implanters, and we expect to maintain our leadership in the high energy segment through sales of both our legacy multi wafer high energy systems and the Purion XE, the Purion EXE and the Purion VXE.

- Medium Current Implant. Our Purion M medium current system offers higher productivity and lower electrical energy consumption compared to competitive offerings, in addition to other advantages. Our Purion M systems also offer differentiated capabilities for specialty applications.
- High Current Implant. Our Purion H spot beam, high current system covers all traditional high current requirements as well as those associated with emerging and future devices. Purion H capabilities extend beyond traditional high current energy and dose ranges, in order to cover new device fabrication requirements as well as to maximize capital utilization and flexibility. In addition, Purion H provides advantages for material modification applications, including those requiring hot and cold implant capabilities.

We believe our ion implant products will continue to meet customer demand for advantages in productivity, process performance and technical extendibility.

Aftermarket Support and Services

Through our Customer Support and Innovation (“CS&I”), business, we offer our customers extensive aftermarket service and support throughout the lifecycle of the equipment we manufacture. We believe that approximately 3,200 of our products are in use in 31 countries worldwide. The service and support that we provide includes used tools, spare parts, equipment upgrades, and maintenance services. We offer varying levels of sales, service and applications support out of our field offices to customers located in 31 countries. Revenue generated through our CS&I business represented 36.6%, 36.0% and 47.8% of revenue in 2018, 2017 and 2016, respectively.

To support our aftermarket business, we have sales and marketing personnel, field service engineers, and spare parts and applications engineers, as well as employees located at our manufacturing facilities who work with our customers to provide customer training and documentation, product, process and applications support.

Most of our customers maintain spare parts inventories for our machines. In addition to our web based spare parts management and replenishment tracking program, we offer a number of Business to Business options to support our customers’ parts management requirements. Our Axcelis Managed Inventory service offering, a parts consignment arrangement, provides the customer with full spares support, with Axcelis retaining responsibility for the complete supply chain. These services provide ease of use alternatives that help us reduce order fulfillment costs and improve cycle time, resulting in an expanded customer base for this service offering.

Sales and Marketing

We primarily sell our equipment and services through our direct sales force. We conduct sales and marketing activities from our sales offices located in the United States, Taiwan, South Korea, China, Germany, Singapore, Japan and Italy. In February 2018, we entered into a distribution and service agreement with SCREEN Semiconductor Solutions, a subsidiary of SCREEN Holdings Co. Ltd., for our Purion ion implant product line in Japan.

International revenue, including export sales from our U.S. manufacturing facilities to foreign customers and sales by foreign subsidiaries and branches, accounted for 87.7%, 84.9% and 80.0% of total revenue in 2018, 2017 and 2016, respectively. Substantially all of our sales are denominated in U.S. dollars. See Note 17 to our Consolidated Financial Statements contained in Item 15 of this Form 10-K for a breakdown of our revenue and long lived assets in the United States, Europe and Asia. See also Item 1A, “Risk Factors,” for information about risks attendant to our foreign operations.

Customers

In 2018, the top 20 semiconductor chip manufacturers accounted for approximately 88.8% of total semiconductor capital equipment spending, down from 90.9% in 2017. These manufacturers are from the largest semiconductor chip manufacturing regions in the world: the United States, Asia Pacific (Taiwan, South Korea, Singapore, Japan and China) and Europe.

Information on net sales to unaffiliated customers is included in Note 2 of Notes to Consolidated Financial Statements. For the year ended December 31, 2018, revenues from each of Samsung Electronics Co, Ltd., and SK hynix represented 10 percent or more of consolidated revenues and the loss of these customers would have a material adverse effect on our business.

Research and Development

Our industry continues to experience rapid technological change, requiring us to frequently introduce new products and enhancements. Our Beverly, Massachusetts Advanced Technology Center houses a process development

laboratory with 12,500 sq. ft. of class 10/100/1000 clean room for product demonstrations and process development and a 34,000 sq. ft. customer training center. The Advanced Technology Center provides infrastructure and process capabilities that allow customers to test their unique process steps on our systems under conditions that substantially replicate the customers' production environments. This facility also provides significant capability for our research and development efforts.

We devote a significant portion of our personnel and financial resources to research and development programs and seek to maintain close relationships with our customers to remain responsive to their product needs. We have also sought to reduce the development cycle for new products through a collaborative process whereby our engineering, manufacturing and marketing personnel work closely together with one another and with our customers at an earlier stage in the process. We use 3D, computer aided design, finite element analysis and other computer based modeling methods to test new designs.

Our expenses for research and development were \$51.9 million, \$43.1 million and \$34.4 million in 2018, 2017 and 2016, respectively, or 11.7%, 10.5% and 12.9% of revenue, respectively. We expect that research and development expenditures will continue to represent a similar level of investment in future years.

Manufacturing

We manufacture products at our 417,000 sq. ft. ISO 9001:2015, ISO 14001:2015 certified plant in Beverly, Massachusetts. Our facility employs best in class manufacturing techniques, including lean manufacturing, six sigma controls and advanced inventory management, purchasing and quality systems.

Our clean manufacturing process uses class 1,000/10,000 space to facilitate most of our manufacturing requirements.

Our core competency in manufacturing and supply chain management is built around system assembly and testing, which remains an in house capability due to the high degree of expertise and intellectual property associated with the process and design. Non core work is sourced to one of several global partners and includes items such as vacuum systems, wafer handling and commodity level components. We continuously pursue outsourcing opportunities where the economics are justified, with a goal of enabling quality and margin improvement. Our supply chain team is globally focused and is located in Beverly and Singapore. Customized and commercially available software solutions drive our planning, purchasing and inventory tracking process.

Our products are designed to be assembled and tested in a modular fashion, which facilitates our industry recognized "ship from cell" process. Specially developed test stands, software and tooling provide the framework for this accelerated delivery process. Customers that choose ship from cell substantially improve their delivery times while receiving the same high level of quality provided by more traditional longer cycle integration techniques. Product margins and

inventory turns also improve as a result of shorter factory cycle times and increased labor productivity.

Installation of our equipment is provided by factory and field teams. The process includes assembling the equipment at our installation site, and after it has been connected, recalibrating it to factory specifications.

Competition

The semiconductor industry is highly competitive and is characterized by a small number of participants ranging in size. Significant competitive factors in the semiconductor capital equipment market include price, cost of ownership, equipment performance, customer support, capabilities and breadth of product line.

In ion implantation, we mainly compete against Applied Materials, Inc. Applied Materials and Axcelis are the only ion implant manufacturers with a full range of implant products, and service and support infrastructures able to service our customers globally. Three other niche players we compete with from time to time include Advanced Ion Beam Technology, Inc., Nissin Ion Implantation Co., Ltd. and Sumitomo Heavy Industries Ion Technology Co., Ltd.

Intellectual Property

We rely on patent, copyright, trademark and trade secret protection in the United States and in other countries, as well as contractual restrictions, to protect our proprietary rights in our products and our business. As of January 1, 2019, we had 243 active patents issued in the United States and 491 active patents granted in other countries, as well as 216 patent applications (48 in the United States and 168 in other countries) on file with various patent agencies worldwide. Patents are generally in effect for up to 20 years from the filing of the application.

We intend to file additional patent applications and grow our intellectual property portfolio as appropriate. Although patents are important to our business, we do not believe that we are substantially dependent on any single patent or any group of patents.

We have trademarks, both registered and unregistered, that are maintained to provide customer recognition for our products in the marketplace. Trademark registrations generally remain in effect as long as the trademarks are in use. From time to time, we enter into license agreements with third parties under which we obtain or grant rights to patented or proprietary technology. We do not believe that any of our licenses are currently material to us.

Backlog

Systems backlog, including deferred systems revenue, was \$65.1 million and \$87.3 million as of December 31, 2018 and 2017, respectively. We believe it is meaningful to investors to include deferred systems revenue as part of our backlog. Deferred systems revenue represents revenue that will be recognized in future periods based on prior shipments or customer prepayments. Our policy is to include in backlog only those system orders for which we have accepted purchase orders and are typically due to ship within six months. All orders are subject to cancellations or rescheduling by customers with limited or no penalties.

Backlog does not include orders received and fulfilled within a quarter. Our backlog at the beginning of a quarter typically does not include all orders required to achieve our sales objectives for that quarter. Backlog is not necessarily an indicator of future business trends because orders for services or parts received during the quarter are generally performed or shipped within the same quarter.

Bookings in the quarter ended December 31, 2018 were \$42.1 million compared to \$103.8 million in the quarter ended December 31, 2017.

Employees

As of December 31, 2018, we had 992 employees and 87 temporary staff worldwide, of which 761 work in North America, 261 in Asia and 57 in Europe. We consider our relationship with our employees to be good. Our employees are not represented by a labor union and are not subject to a collective bargaining agreement. One of our European locations has formed a work council, which has certain information and discussion rights under applicable law.

Environmental

We are subject to environmental laws and regulations in the countries in which we operate that regulate, among other things: air emissions; water discharges; and the generation, use, storage, transportation, handling and disposal of solid and hazardous wastes produced by our manufacturing, research and development and sales activities. As with other companies engaged in like businesses, the nature of our operations exposes us to the risk of environmental liabilities, claims, penalties and orders.

We are proud of our commitment to improving our environment. We believe that our operations are in substantial compliance with applicable environmental laws and regulations and that there are no pending environmental matters that would have a material impact on our business. We are ISO 9001:2015 and ISO 14001:2015 certified at our Beverly, MA facility.

Executive Officers of the Registrant

Mary G. Puma, 61, has been our President and Chief Executive Officer since January 2002, having served as Chairman from 2005 to 2015. From May 2000 until January 2002, Ms. Puma was our President and Chief Operating Officer. In 1998, she became General Manager and Vice President of the Implant Systems Division of Eaton Corporation, a global diversified industrial manufacturer. In May 1996, she joined Eaton as General Manager of the Commercial Controls Division. Prior to joining Eaton, Ms. Puma spent 15 years in various marketing and general management positions for General Electric Company. Ms. Puma is a director of Nordson Corporation and Semiconductor Equipment and Materials International (SEMI).

Kevin J. Brewer, 60, became our Executive Vice President and Chief Financial Officer in September 2013, having served as interim Chief Financial Officer beginning in June 2013. Mr. Brewer also manages our Global Operations. Mr. Brewer had been our Executive Vice President, Global Operations since 2008 and our Senior Vice President, Manufacturing Operations since May 2005, prior to which he had been Vice President of Manufacturing Operations since October 2002 and Director of Operations from 1999 to 2002. Prior to joining Axcelis in 1999, Mr. Brewer was Director of Operations, Business Jets at Raytheon Aircraft Company, a leading manufacturer of business and special mission aircraft owned by Raytheon Company, a manufacturer of defense, government and commercial electronics, as well as aircraft. Prior to that, Mr. Brewer held various management positions in operations and strategic planning in Raytheon Company's Electronic Systems and Missile Systems groups.

John E. Aldeborgh, 62, has been our Executive Vice President, Customer Operations since February 2013, having joined Axcelis in January 2013 as our Senior Vice President, Customer Operations. Prior to joining Axcelis, Mr. Aldeborgh served as the Chief Executive Officer and President, and as a Director, of innoPad, Inc., a privately held manufacturer of Chemical Mechanical Planarization pads, since 2006. Mr. Aldeborgh served in various marketing and sales position at Varian Semiconductor Equipment Associates Inc. (an ion implantation systems business acquired by Applied Materials Inc. in 2011) from 2002 to 2005, including Vice President of Sales and Marketing. Prior to Varian, Mr. Aldeborgh served as President and Chief Operating Officer of Ebara Technologies, Inc., from 1998 to 2002. Mr. Aldeborgh also held various positions at Genus, Inc. from 1989 to 1998, including Executive Vice President and Chief Operating Officer.

William Bintz, 62, is our Executive Vice President, Product Development since November 2016. From 2011 until November 2016, Mr. Bintz served as Executive Vice President, Product Development, Engineering and Marketing. Prior to that, he served as Senior Vice President, Marketing beginning in September 2007, after joining Axcelis in early 2006 as Director of Marketing for curing and cleaning products and shortly thereafter becoming Vice President of Product Marketing. Prior to joining Axcelis, from 2002 Mr. Bintz was Product Director for Medium Current and High Energy Ion Implant System at Varian Semiconductor Equipment Associates, Inc. Before that, he was General Manager of the Materials Delivery Products Group at MKS Instruments, beginning in 1999, and General Manager of the Thermal Processing Systems Division at Eaton Corporation (now Axcelis) beginning in 1995.

Lynnette C. Fallon, 59, is our Executive Vice President, Human Resources/Legal and General Counsel, a position she has held since May 2005. Prior to that, Ms. Fallon was Senior Vice President HR/Legal and General Counsel since 2002, and Senior Vice President and General Counsel since 2001. Ms. Fallon has also been our corporate Secretary since 2001. Before joining Axcelis, Ms. Fallon was a partner in the Boston law firm of Palmer & Dodge LLP since 1992, where she was head of the Business Law Department from 1997 to 2001.

Douglas A. Lawson, 58, has been our Executive Vice President, Corporate Marketing and Strategy since November 2013, having joined Axcelis as Vice President Business Development in 2010, and holding the position of Senior Vice President of Strategic Initiatives beginning in 2011. Mr. Lawson also manages our Information Technology function. Prior to joining the Company in 2010, he held the position of General Manager of Luminus Devices from 2009 to 2010. He has over 30 years of experience in the technology industry, and has held numerous executive and technical positions at BTU International, PRI Automation, Digital Equipment and Intel.

Russell J. Low, Ph. D., 48, is our Executive Vice President, Engineering, having joined Axcelis in October 2016. Prior to joining the Company, Dr. Low held the position of Vice President of Engineering, MOCVD Business Unit at Veeco Instruments since 2013, prior to which he was Veeco's Senior Director of Engineering, Molecular Beam Epitaxy Business Unit beginning in 2012. From 2003 to 2012, Dr. Low held a number of positions at Varian Semiconductor Equipment Associates, most recently as Director of Technology. Prior to that, Dr. Low held engineering positions in the thermal processing and ion implant divisions of Applied Materials, Inc. from 1997 to 2003.

Item 1A. Risk Factors.

Risks Related to Our Business and Industry

Set forth below and elsewhere in this Form 10-K and in other documents we file with the SEC are risks and uncertainties that could cause actual results to differ materially from the results contemplated by the forward looking statements contained in this Form 10-K. It is not possible to predict or identify all such risk factors. Consequently, the following is not a complete discussion of all potential risks or uncertainties.

If semiconductor chip manufacturers do not make sufficient capital expenditures, our sales and profitability will be harmed.

New systems orders and used tool sales depend upon demand from semiconductor chip manufacturers who build or expand fabrication facilities. When the rate of construction or expansion of fabrication facilities declines, demand for our systems will decline, reducing our revenue. In addition, all or a portion of the demand for increased capacity may be satisfied by a semiconductor chip manufacturer's ability to reconfigure and re-use equipment they already own. Revenue decline also hurts our profitability because our established cost structure and our continued investments in engineering, research and development and marketing necessary to develop new products and to maintain extensive customer service and support capabilities limit our ability to reduce expenses in proportion to declining sales.

If we fail to develop and introduce reliable new or enhanced products and services that meet the needs of semiconductor chip manufacturers, our results will suffer.

Rapid technological changes in semiconductor chip manufacturing processes require us to respond quickly to changing customer requirements. Our future success will depend in part upon our ability to develop, manufacture and successfully introduce new systems and product lines with improved capabilities. This will depend upon a variety of factors, including new product selection, timely and efficient completion of product design and development as well as manufacturing and assembly processes, product performance in the field and effective sales and marketing. In particular:

- We must continue to develop competitive technical specifications for new systems, or enhancements to our existing systems, and manufacture and ship these systems or enhancements in volume in a timely manner.
- We will need to accurately predict the schedule on which our customers will be ready to transition to new products, in order to accurately forecast demand for new products while managing the transition from older products.

- We will need to effectively manage product reliability or quality problems that often exist with new systems, in order to avoid higher manufacturing costs, delays in acceptance and payment and additional service and warranty expenses, and ultimately, a lack of repeat orders.
- Our new products must be accepted in the marketplace.

Our failure to meet any of these requirements will have a material adverse effect on our operating results and profitability.

A significant portion of our revenue depends on customers electing to buy aftermarket products and services from Axcelis.

Historically, a significant portion of our product revenue and all of our service revenue relates to our sale of “aftermarket” products and services, which include parts, consumables, upgrades, service contracts, and time and materials billings. Some of our customers purchase fewer aftermarket products and services, often training their own staff to maintain and service semiconductor capital equipment rather than relying on the equipment manufacturer for these services. In addition, we compete against third party parts suppliers for the sale of parts and consumables that are

not protected by patents or otherwise proprietary. To the extent our customers purchase parts and services from other vendors or provide their own system maintenance labor, our revenue and profitability will be less.

Our financial results may fluctuate significantly.

We derive our new systems revenue from the sale of a small number of expensive products to a relatively small number of customers. The selling prices on our ion implant and other systems range from approximately \$2.0 million to \$8.0 million. We also sell used equipment in our aftermarket business. Each sale, or failure to make a sale, may have a significant effect on us in a particular quarter. In a given quarter, a number of factors can adversely affect our revenue and results, including changes in our product mix, increased fixed expenses per unit due to reductions in the number of products manufactured, and higher fixed costs due to increased levels of research and development and expansion of our worldwide sales and marketing organization. Our financial results also fluctuate based on gross profit realized on sales. A variety of factors may cause gross profit as a percentage of revenue to vary, including the mix and average selling prices of products sold, costs to manufacture and customize systems, warranty costs and impact of changes to inventory reserves. New product introductions may also affect our gross margin. Fluctuations in our financial results may have an adverse effect on the price of our common stock.

Our financial results may fall short of anticipated levels because forecasting revenue and profitability is complex and may be inaccurate.

Management may from time to time provide financial forecasts to investors. These forecasts are based on assumptions, which are believed to be reasonable when made, of the timing of system orders, system shipments, system acceptance and aftermarket revenue. Any of these assumptions can prove erroneous and the level of revenue recognizable in a particular quarter may vary from the forecast. Our lengthy sales cycle, coupled with customers' competing capital budget considerations, make revenue difficult to predict. In addition, our backlog at the beginning of a quarter typically does not include all orders required to achieve our sales objectives for that quarter and is not a reliable indicator of our future sales. As a result, our revenue and operating results for a quarter depend on our shipping systems on previous orders as scheduled during that quarter, receiving customer acceptance of previously shipped products, and obtaining new orders for products and services to be provided in that same quarter. Any delay in, or cancellation of, scheduled shipments and customer acceptances or in revenue from new orders, including aftermarket revenue, could materially affect our financial results.

Accounting rules addressing revenue recognition add more complexity in forecasting quarterly revenue and profitability. Orders for our products usually contain multiple performance obligations that result in revenue deferral under generally accepted accounting principles. Due to the foregoing factors, investors should understand that our actual financial results for a quarter may vary significantly from our forecasts of financial performance for that quarter. Failure to meet forecasted financial performance may have an adverse effect on the price of our common stock.

The semiconductor industry is cyclical and we expect that demand for our products will increase and decrease, making it difficult to manage the business and potentially causing harm to our sales and profitability.

The semiconductor industry is cyclical, experiencing upturns when the demand for our products is high and downturns when our customers are not investing in new or expanded fabrication facilities. From time to time, inventory buildups in the semiconductor industry, produce an oversupply of semiconductors. This can cause a reduced demand for capital equipment such as our products, negatively impacting our sales and level of profitability. Our revenue can vary significantly from one point in the cycle to another, making it difficult to manage the business, both when revenue is increasing and when it is decreasing. In addition, a substantial portion of our operating expenses do not fluctuate with changes in volume. Significant decreases in revenue can therefore have a disproportionate effect on profitability. In addition, reduced demand for our products and services may require Axcelis to implement cost reduction efforts, including restructuring activities, which may adversely affect Axcelis' ability to capitalize on opportunities that arise in the future.

If we fail to compete successfully in the highly competitive semiconductor capital equipment industry, our sales and profitability will decline.

The ion implant segment is highly competitive and includes one company with substantially greater financial, engineering, manufacturing, marketing and customer service and support resources that may better position it to compete successfully, as well as several smaller companies that could provide innovative systems with technology that may have performance advantages. We expect our competitors to continue to improve the design and performance of their existing products and processes and to introduce new products and processes with improved price and performance characteristics. If we are unable to improve or introduce competing products when demanded by the markets, our business will be harmed. Finally, if we must lower prices to remain competitive without commensurate cost of goods savings, our gross margin and profitability will be adversely affected.

We are dependent on sales to a limited number of large customers; the loss of a significant customer or any reduction in orders from them could materially affect our sales.

Historically, we have sold a significant portion of our products and services to a limited number of semiconductor chip manufacturers. In 2018, our top ten customers accounted for 76.9% of our net sales, in comparison to 73.3% and 70.2% in 2017 and 2016, respectively. None of our customers have entered into a long term agreement requiring it to purchase our products. Although the composition of the group comprising our largest customers has varied from year to year, the loss of a significant customer or any reduction or delays in orders from any significant customer will adversely affect us. Consolidation of semiconductor chip manufacturers may result in the loss of a customer.

Axcelis is subject to the risks of operating internationally: we derive a substantial portion of our revenue from outside the United States, especially from Asia.

We are substantially dependent on sales of our products and services to customers outside the United States. International sales, including export sales from our U.S. manufacturing facilities to non U.S. customers and sales by our non U.S. subsidiaries, accounted for 87.7% of total revenue in 2018 in comparison to 84.9% of total revenue in 2017 and 80.0% in 2016. Ion implanter system shipments to Asian customers represented 86.6% of total system shipment dollars in 2018 in comparison to 82.6% in 2017 and 75.3% in 2016. We anticipate that international sales will continue to account for a significant portion of our revenue. The potential increased investment in semiconductor chip manufacturing capability in China is expected to result in both risk and opportunity. Because of our dependence upon international sales, our results and prospects may be adversely affected by a number of factors, including:

- unexpected changes in laws or regulations resulting in more burdensome governmental controls, tariffs, restrictions, embargoes or export license requirements;
- volatility in currency exchange rates;

- political and economic instability;
- difficulties in accounts receivable collections;
- extended payment terms beyond those customarily offered in the United States;
- difficulties in managing suppliers, service providers or representatives outside the United States;
- difficulties in staffing and managing foreign subsidiary operations; and
- potential adverse tax consequences.

We may not be able to maintain and expand our business if we are not able to hire, retain and integrate qualified personnel.

Our business depends on our ability to attract and retain qualified, experienced employees. There is substantial competition for experienced engineering, technical, financial, sales and marketing personnel in our industry. In particular, we must attract and retain highly skilled design and process engineers. Competition for such personnel is intense, particularly in the Boston metropolitan area, as well as in other locations around the world. If we are unable to retain our existing key personnel, or attract and retain additional qualified personnel, we may from time to time experience insufficient levels of staffing to fully develop, manufacture and market our products and perform services for our customers. As a result, our growth could be limited or we could fail to meet our delivery commitments or experience deterioration in service levels or decreased customer satisfaction, all of which could adversely affect our financial results.

Our dependence upon suppliers for many components and sub assemblies could result in increased costs or delays in the manufacture and sale of our products.

We rely to a substantial extent on outside vendors to manufacture many of the components and sub assemblies of our products. We obtain many of these components and sub assemblies from a limited group of suppliers. Accordingly, based on situations outside of our control, we may be unable to obtain an adequate supply of required components on a timely basis, on price and other terms acceptable to us, or at all. In addition, we often quote prices to our customers and accept customer orders for our products before purchasing components and sub assemblies from our suppliers. If our suppliers increase the cost of components or sub assemblies, we may not have alternative sources of supply and may not be able to raise the price of our products to cover all or part of the increased cost of components, negatively impacting our gross margin.

The manufacture of some of these components and sub assemblies is an extremely complex process and requires long lead times. As a result we could experience delays or shortages. If we are unable to obtain adequate and timely deliveries of our required components or sub assemblies, we may have to seek alternative sources of supply or manufacture these components internally. This could delay our ability to manufacture or to ship our systems on a timely basis, causing us to lose sales, incur additional costs, delay new product introductions and suffer harm to our reputation.

Moreover, if actual demand for Axcelis' products is different than expected, Axcelis may purchase more or fewer parts than necessary or incur costs for canceling, postponing or expediting delivery of parts. If Axcelis purchases inventory in anticipation of customer demand that does not materialize, or if customers reduce or delay orders, Axcelis may incur excess inventory charges.

Our international operations involve currency risk.

Substantially all of our sales are billed in U.S. dollars, thereby reducing the impact of fluctuations in foreign exchange rates on our results. However, the aftermarket revenues of our non-U.S. subsidiaries, and most of the operating expenses of these non-U.S. subsidiaries, are received and incurred in local currencies. The translation of these operating results into U.S. dollars in our Consolidated Statement of Operations can result in other income (expense). Similarly, the translation of asset and liability values to U.S. dollars are recorded in stockholders' equity as an element of accumulated other comprehensive income (loss). Accordingly, fluctuations in exchange rates can impact reported revenues, expense, and profitability and asset values in our Consolidated Financial Statements. During the year ended December 31, 2018, approximately 22.5% of our revenue was derived in local currencies from foreign operations with this inherent risk. In addition, at December 31, 2018, our operations outside of the United States accounted for approximately 12.9% of our total assets, the majority of which was denominated in currencies other than the U.S. dollar.

Axcelis is exposed to risks related to cybersecurity threats and incidents.

In the conduct of our business, Axcelis collects, uses, transmits and stores data on information technology systems. This data includes confidential information belonging to Axcelis, our employees or our customers or other business partners, some of which is personally-identifiable information of individuals. As reported in the 2017 Verizon Data Breach Investigation Report, attempts to access confidential business information make up almost all of the cyber

security risk for a manufacturing company, with 93% of the threat actors external to the targeted company. Verizon reported that most of the attacks are conducted by state-affiliated actors who are an “advanced persistent threat.” Axcelis has been and expects to be subject to cybersecurity threats and incidents, including employee error or misuse; individual attempts to gain unauthorized access to information systems; and sophisticated and targeted measures known as advanced persistent threats, none of which have had a material impact on the Company to date. Axcelis devotes significant resources to network security, data encryption, employee training and other measures to protect our systems and data from unauthorized access or misuse. However, depending on their nature and scope, cybersecurity incidents could result in business disruption; the misappropriation, corruption or loss of confidential information and critical data (Axcelis’ and that of third parties); reputational damage; litigation with third parties; diminution in the value of Axcelis’ investment in research, development and engineering; data privacy issues; and increased cybersecurity protection and remediation costs. These adverse outcomes could negatively impact our revenues, expenses, profitability and asset values.

Our proprietary technology may be vulnerable to efforts by competitors to challenge or design around, potentially reducing our market share.

We rely on a combination of patents, copyrights, trademark and trade secret laws, non-disclosure agreements and other intellectual property protection methods to protect our proprietary technology. Despite our efforts to protect our intellectual property, our competitors may be able to challenge, design around or legitimately use the proprietary technology embedded in our systems or other technology or information used in our business. If this occurs, the value of our proprietary technology will be diminished. Our means of protecting our proprietary rights may not be adequate and our patents may not be sufficient to prevent others from using technology that is similar to or the same as our technology. Patents issued to us may be challenged, and might be invalidated or circumvented and any rights granted under our patents may not provide adequate protection to us. Our competitors may independently develop similar technology, duplicate features of our products or design around patents that may be issued to us. As a result of these threats to our proprietary technology, we may have to resort to costly litigation to enforce or defend our intellectual property rights. Finally, all patents expire after a period of time (in the U.S., patents expire 20 years from the date of filing of the patent application). Our market share could be negatively impacted by the invalidation or expiration of a patent which had created a barrier for our competitors.

Axcelis also has agreements with third parties for licensing of patented or proprietary technology with Axcelis as the licensor or the licensee. Termination of license agreements or claims of infringement with respect to such technology could have an adverse impact on our financial performance or ability to ship products with existing configurations.

We (or customers that we indemnify) might face intellectual property infringement claims or patent disputes that may be costly to resolve and, if resolved against us, could be very costly to us and prevent us from making and selling our systems.

From time to time, claims and proceedings may be asserted against us relative to patent validity or infringement matters. We typically agree to indemnify our customers from liability to third parties for intellectual property infringement arising from the use of our products in their intended manner. Therefore, we may receive notification

from customers who believe that we owe them indemnification or other obligations related to infringement claims made against the customers by third parties. Our involvement in any patent dispute or other intellectual property dispute or action to protect trade secrets, even if the claims are without merit, could be very expensive and could divert the attention of our management. Adverse determinations in any litigation could subject us to significant liabilities to third parties, require us to remove certain features from our products or seek costly licenses from third parties or prevent us from manufacturing and selling our systems. In addition, infringement indemnification clauses in system sale agreements may require us to take other actions or require us to provide certain remedies to customers who are exposed to indemnified liabilities. Any of these situations could have a material adverse effect on our business results.

If operations were disrupted at Axcelis' primary manufacturing facility, it would have a negative impact on our business.

We have one primary manufacturing facility located in Massachusetts. Our operations could be subject to disruption for a variety of reasons, including, but not limited to natural disasters, work stoppages, operational facility constraints and terrorism. Such disruption could cause delays in shipments of products to our customers and could result in cancellation of orders or loss of customers, which could seriously harm our business.

If we do not have access to capital on favorable terms, on the timeline we anticipate, or at all, our financial condition and results of operations could be materially adversely affected.

We require a substantial amount of capital to meet our operating requirements and remain competitive. We routinely incur significant costs to purchase inventory to meet expected system sales, to develop and introduce new products, and to place evaluation systems at new customer sites. Our Board has also authorized management to repurchase shares of our common stock under a one year stock repurchase program. There can be no assurance that we will realize a return on the capital expended. Although our current cash levels are expected to be adequate for our foreseeable cash requirements, if our operating results falter, or our cash flow or capital resources prove inadequate, we may incur debt to fund these requirements. Significant volatility or disruption in the global financial markets may result in us not being able to obtain additional financing on favorable terms, on the timeline we anticipate, or at all, and we may not be able to refinance, if necessary, any outstanding debt when due, all of which could have a material adverse effect on our financial condition. Any inability to obtain funding on favorable terms, on the timeline we anticipate, or at all, may cause us to curtail our operations significantly, reduce planned capital expenditures and research and development, or obtain funds through arrangements that management does not currently anticipate, including disposing of our assets and relinquishing rights to certain technologies, the occurrence of any of which may significantly impair our ability to remain competitive, and materially and adversely affect our results of operations and financial condition.

The market price of our common stock may be volatile, which could result in substantial losses for investors.

The stock markets in general, and the markets for semiconductor equipment stocks in particular, have experienced extreme volatility that has often been unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the trading price of our common stock.

The market price of the common stock may also fluctuate significantly in response to the following factors, among others, some of which are beyond our control:

- variations in our quarterly operating results;

- the issuance or repurchase of shares of our common stock;
- changes in securities analysts' estimates of our financial performance;
- changes in market valuations of similar companies;
- announcements by us or our competitors of significant contracts, acquisitions, strategic partnerships, joint ventures, capital commitments, new products or product enhancements;
- loss of a major customer or failure to complete significant transactions; and
- additions or departures of key personnel.

The trading price of our common stock in the past has had significant volatility, and we cannot accurately predict every potential risk that may materially and adversely affect our stock price.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

We lease our principal facility in Beverly, Massachusetts, which comprises 417,000 square feet. The facility is principally used for manufacturing, research and development, sales/marketing, customer support, advanced process development, product demonstration, customer training center and corporate headquarters. We believe that our manufacturing facilities and equipment generally are well maintained, in good operating condition, suitable for our purposes, and adequate for our present operations.

We own 23 acres of undeveloped property in Beverly, Massachusetts, adjacent to our headquarters.

As of December 31, 2018, we also leased 45 other properties, of which 11 are located in the United States and the remainder are located in Asia and Europe, including offices in Taiwan, Singapore, South Korea, China, Malaysia, Japan, Italy and Germany. These properties are used for sales and service offices and warehousing.

Our Beverly, Massachusetts facility is ISO 9001:2015 and ISO 14001:2015 and our European office is ISO 9001:2015 certified.

Item 3. Legal Proceedings.

We are not presently a party to any litigation that we believe might have a material adverse effect on our business operations. We are, from time to time, a party to litigation that arises in the normal course of our business operations.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Our common stock trades on the Nasdaq Global Select Market under the symbol ACLS. As of March 4, 2019, we had approximately 1,500 stockholders of record. We have never paid any cash dividends to our stockholders and do not anticipate paying cash dividends in the foreseeable future. The remainder of the information required by Item 5 of Form 10-K is incorporated by reference to the information responsive thereto contained in the section of the Axcelis Proxy Statement for the Annual Meeting of Stockholders to be held May 14, 2019 captioned “Proposal 2: Approval of Amendment to the 2012 Equity Incentive Plan – Current Equity Compensation Plan Information.”

Item 6. Selected Financial Data.

The following selected consolidated statements of operations data for each of the three years ended December 31, 2018, 2017 and 2016 and the consolidated balance sheets data as of December 31, 2018 and 2017 have been derived from the audited consolidated financial statements contained in Item 15 of Part IV of this Form 10 K. The selected consolidated balance sheets data as of December 31, 2016 and 2015, and the statements of operations data for the years ended December 31, 2015 and 2014, have been derived from the audited financial statements contained in our Form 10 K filed on March 14, 2017. The consolidated balance sheets data as of December 31, 2014 have been derived from the audited financial statements contained in our Form 10-K filed on March 4, 2016.

The historical financial information set forth below may not be indicative of our future performance and should be read together with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our historical consolidated financial statements and notes to those statements included in Item 7 of Part II and Item 15 of Part IV, respectively, of this Form 10 K.

	Year ended December 31,				
	2018*	2017	2016	2015	2014
	(In thousands, except per share amounts)				
Consolidated statements of operations data:					
Revenue	\$ 442,575	\$ 410,561	\$ 266,980	\$ 301,495	\$ 203,051
Gross profit	179,636	150,247	99,598	101,706	70,164
Income (loss) from operations	59,959	47,842	16,623	20,718	(10,661)
Income (loss) before income taxes	54,705	43,831	11,024	15,205	(10,167)
Net income (loss)	45,885	126,959	11,001	14,678	(11,266)
Net income (loss) per share:					

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Basic	\$ 1.42	\$ 4.11	\$ 0.38	\$ 0.51	\$ (0.40)
Diluted	\$ 1.35	\$ 3.80	\$ 0.36	\$ 0.49	\$ (0.40)
Shares used in computing basic and diluted per share amounts:					
Basic	32,286	30,866	29,195	28,595	27,863
Diluted	34,002	33,436	30,947	30,229	27,863
Consolidated balance sheets data:					
Cash and cash equivalents	\$ 177,993	\$ 133,407	\$ 70,791	\$ 78,889	\$ 30,753
Working capital	311,774	260,488	192,998	185,589	126,541
Total assets	548,441	488,218	302,231	281,784	221,158
Long-term liabilities	55,107	55,321	53,045	53,652	7,204
Stockholders' equity	408,337	353,610	201,455	183,764	161,856

* The adoption of ASC 606 on January 1, 2018 resulted in increases to revenue of \$1.0 million, to net income of \$0.9 million and basic and diluted earnings per share of \$0.03 for the twelve months ended December 31, 2018.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Certain statements in "Management's Discussion and Analysis of Financial Condition and Results of Operations" are forward looking statements that involve risks and uncertainties. Words such as may, will, should, would, anticipates, expects, intends, plans, believes, seeks, estimates and similar expressions identify such forward looking statements. The forward looking statements contained herein are based on current expectations and entail various risks and uncertainties that could cause actual results to differ materially from those expressed in such forward looking statements. Factors that might cause such a difference include, among other things, those set forth under "Liquidity and Capital Resources" and "Risk Factors" and others discussed elsewhere in this Form 10 K. Readers are cautioned not to place undue reliance on these forward looking statements, which reflect management's analysis only as of the date hereof. We assume no obligation to update these forward looking statements to reflect actual results or changes in factors or assumptions affecting forward looking statements, except as may be required by law.

Overview

The semiconductor capital equipment industry is subject to cyclical swings in capital spending by semiconductor chip manufacturers. Capital spending is influenced by demand for semiconductors and the products using them, the utilization rate and capacity of existing semiconductor chip manufacturing facilities and changes in semiconductor technology, all of which are outside of our control. As a result, our revenue may fluctuate from year to year and period to period. Our established cost structure does not vary significantly with changes in volume. We may also experience fluctuations in operating results and cash flows depending on our revenue level.

Despite a significant slowdown in memory spending in the second half of 2018, revenue increased by nearly 8% over 2017, with systems revenue increasing by 6.7%, and revenues from Customer Support & Innovation ("CS&I"), our aftermarket business, increasing by nearly 10%. 2018 full year gross margin exceeded 40% and cash increased by 33% to nearly \$178 million.

Our 2018 results were the product of hard work across the Company over prior years to expand the Purion install base to a large and diverse group of customers. We have focused on key markets in the mature process technology sector such as image sensor, power device and mature foundry and logic. We developed Purion product extensions specifically for these markets, becoming key partners with these customers. As a result, our fourth quarter 2018 revenues showed a split of 68% mature process technology and 32% memory, illustrating our expansion into the mature process technology sector, and the reduction in our dependence on memory customers. For the full year the mix was 54% mature process technology and 46% memory.

We also continued to work diligently to ensure that manufacturing and operating expense levels remain well aligned to business conditions.

The market for our systems and aftermarket products and services is represented by a relatively small number of companies. In 2018, the top 20 semiconductor chip manufacturers accounted for approximately 88.8% of total semiconductor capital equipment spending, down from 90.9% in 2017. Our net revenue from our ten largest customers accounted for 76.9% of total revenue for the year ended December 31, 2018 compared to 73.3% and 70.2% of revenue for the years ended December 31, 2017 and 2016, respectively. For the year ended December 31, 2018, we had two customers representing 20.1% and 12.1% of total revenue, respectively.

Critical Accounting Estimates

Management's discussion and analysis of our financial condition and results of operations are based upon Axcelis' consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an on going basis, we evaluate our estimates and assumptions. Management's estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and

liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following accounting policies are critical in the portrayal of our financial condition and results of operations and require management's most significant judgments and estimates in the preparation of our consolidated financial statements. For additional accounting policies see Note 2 to the consolidated financial statements for the year ended December 31, 2018 included in this Annual Report on Form 10-K.

Revenue Recognition

Our accounting policies relating to the recognition of revenue require management to make estimates, determinations and judgments based on historical experience and on various other assumptions, which include (i) the existence of a contract with the customer, (ii) the identification of the performance obligations in the contract, (iii) the value of any variable consideration in the contract, (iv) the stand alone selling price of multiple obligations in the contract, for the purpose of allocating the consideration in the contract, and (v) determining when a performance obligation has been met. Our revenue recognition policies are set forth in section (i) of Note 2, Summary of Significant Accounting Policies, to the consolidated financial statements for the year ended December 31, 2018 included in this Annual Report on Form 10-K. Recognition of revenue based on incorrect judgments, including an erroneous allocation of the estimated sales price between the units of accounting, could result in inappropriate recognition of revenue, or incorrect timing of revenue recognition, which could have a material effect on our financial condition and results of operations.

Impairment of Long Lived Assets

We record impairment losses on long lived assets when events and circumstances indicate that these assets might not be recoverable. Recoverability is measured by a comparison of the assets' carrying amount to their expected future undiscounted net cash flows. If such assets are considered to be impaired, the impairment is measured based on the amount by which the carrying value exceeds its fair value.

Actual performance could be materially different from our current forecasts, which could impact estimates of undiscounted cash flows and may result in the impairment of the carrying amount of the long lived assets in the future. This could be caused by strategic decisions made in response to economic and competitive conditions, the impact of the economic environment on our customer base or a material adverse change in our relationships with significant customers.

We did not record an impairment charge in the years ended December 31, 2018, 2017 or 2016.

Accounts Receivable—Allowance for Doubtful Accounts

We record an allowance for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Our allowance for doubtful accounts is established based on a specific assessment of collectability of our customer accounts. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be necessary.

Inventory—Provision for Excess and Obsolescence and Lower of Cost or Net Realizable Value

We record a provision for estimated excess and obsolete inventory and lower of cost or net realizable value. The provision is determined using management's assumptions of materials usage, based on estimates of forecasted and historical demand and market conditions. If actual market conditions become less favorable than those projected by management, additional inventory write downs may be required.

Although we make every effort to ensure the accuracy of our forecasts or product demand and pricing assumptions, any significant unanticipated changes in demand, pricing, or technical developments would significantly impact the value of our inventory and our reported operating results. In the future, if we determine that inventory needs

to be written down, we will recognize such costs in our cost of revenue at the time of such determination. If we subsequently sell product that has previously been written down, our gross margin in that period will be favorably impacted.

Product Warranty

We generally offer a one year warranty for all of our systems, the terms and conditions of which vary depending upon the product sold. For all systems sold, we accrue a liability for the estimated cost of standard warranty at the time of system shipment and defer the portion of systems revenue attributable to the relative fair value of non standard warranty. Costs for non standard warranty are expensed as incurred. Factors that affect our warranty liability include the number of installed units, historical and anticipated product failure rates, material usage and service labor costs. We periodically assess the adequacy of our recorded liability and adjust the amount as necessary.

Stock-based Compensation

Stock based compensation expense for equity awards with service based conditions is estimated as of the grant date based on the fair value of the award and is recognized as expense over the requisite service period, which generally equals the vesting period, based on the number of awards that are expected to vest. The fair value of restricted stock unit grants is determined using the closing price of our common stock on the date of grant. In contrast, estimating the fair value for stock options requires judgment, including the expected term of our stock options, volatility of our stock, expected dividends, risk free interest rates over the expected term of the options and the expected forfeiture rate.

We consider a number of factors when estimating volatility. Our method of estimating expected volatility for all stock options granted relies on a combination of historical and implied volatility. We believe that this blended volatility results in a more accurate estimate of the grant date fair value of employee stock options because it more appropriately reflects the market's current expectations of future volatility.

We may issue stock option grants with vesting based on performance or market conditions, such as the price of our common stock, or, a combination of time, performance or market conditions. The fair values and derived service periods for all grants that have vesting based on performance or market conditions are estimated using the Monte Carlo valuation method. For each stock option grant with vesting based on a combination of time or market conditions, where vesting will occur if either condition is met, the related compensation costs are recognized over the shorter of the explicit service period or the derived service period.

We use the straight line attribution method to recognize expense for stock based awards such that the expense associated with awards is evenly recognized throughout the period.

The amount of stock based compensation recognized is based on the value of the portion of the awards that are ultimately expected to vest. We estimate forfeitures at the time of grant and revise them, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The term “forfeitures” is distinct from “cancellations” or “expirations” and represents only the unvested portion of the surrendered stock based award.

The benefits of tax deductions in excess of recognized compensation cost is reported as a financing cash flow, rather than as an operating cash flow.

Income Taxes

We record income taxes using the asset and liability method. Deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax basis, and net operating loss and tax credit carryforwards.

Our consolidated financial statements contain certain deferred tax assets which have arisen primarily as a result of operating losses, as well as other temporary differences between financial and income tax accounting.

We establish a valuation allowance when it is more likely than not that some portion or all of the deferred tax assets will not be realized. Significant management judgment is required in determining our provision for income taxes, the deferred tax assets and liabilities and any valuation allowance recorded against those net deferred tax assets.

We evaluate the weight of all available evidence such as historical losses, the expected timing of the reversals of existing temporary differences and projected future taxable income to determine whether it is more likely than not that some portion or all of the net deferred income tax assets will not be realized.

Our income tax expense includes the largest amount of tax benefit for an uncertain tax position that is more likely than not to be sustained upon audit based on the technical merits of the tax position. Settlements with tax authorities, the expiration of statutes of limitations for particular tax positions, or obtaining new information on particular tax positions may cause a change to the effective tax rate. We recognize accrued interest related to unrecognized tax benefits as interest expense and penalties as operating expense.

Results of Operations

The following table sets forth our results of operations as a percentage of total revenue:

	Year ended December 31,					
	2018		2017		2016	
Revenue:						
Product	94.0	%	94.3	%	91.5	%
Services	6.0		5.7		8.5	
Total revenue	100		100		100	
Cost of revenue:						
Product	53.4		57.2		55.8	
Services	6.0		6.2		6.9	
Total cost of revenue	59.4		63.4		62.7	
Gross profit	40.6		36.6		37.3	
Operating expenses:						
Research and development	11.7		10.5		12.9	
Sales and marketing	7.8		6.9		8.9	
General and administrative	7.5		7.5		9.2	
Restructuring Charge	—		—		0.1	
Total operating expenses	27.0		24.9		31.1	
Income from operations	13.6		11.7		6.2	
Other (expense) income:						
Interest income	0.5		0.2		0.1	
Interest expense	(1.2)		(1.3)		(1.9)	

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Other, net	(0.6)	0.1	(0.3)
Total other expense	(1.3)	(1.0)	(2.1)
Income before income taxes	12.3	10.7	4.1
Income tax provision (benefit)	1.9	(20.2)	—
Net income	10.4	% 30.9	% 4.1 %

Revenue

The following table sets forth our revenue:

	Year ended December 31, 2018				Period-to-Period Change		Year ended December 31, 2017				Period-to-Period Change					
	2017				\$	%	2016				\$	%				
	(dollars in thousands)															
Revenue:																
Product	\$	415,922	\$	387,124	\$	28,798	7.4	%	\$	387,124	\$	244,295	\$	142,829	58.5	%
Percentage																
of revenue	94.0	%	94.3	%					94.3	%	91.5	%				
Services	26,653		23,437		3,216	13.7	%		23,437		22,685		752	3.3	%	
Percentage																
of revenue	6.0	%	5.7	%					5.7	%	8.5	%				
Total																
revenue	\$	442,575	\$	410,561	\$	32,014	7.8	%	\$	410,561	\$	266,980	\$	143,581	53.8	%

or 5.7% of revenue for 2017. Although services revenue should increase with the expansion of the installed base of systems, it can fluctuate from period to period based on capacity utilization at customers' manufacturing facilities, which affects the need for equipment service.

2017 Compared with 2016

Product

Product revenue was \$387.1 million or 94.3% of revenue in 2017, compared with \$244.3 million, or 91.5% of revenue in 2016. The increase in product revenue in 2017 was primarily driven by an increase in the number of Purion systems sold.

The total amount of deferred revenue at December 31, 2017 and 2016 was \$18.1 million and \$11.0 million, respectively. The increase was primarily due to the increased number of systems sold in the current year.

Services

Services revenue was \$23.4 million, or 5.7% of revenue for 2017, compared with \$22.7 million, or 8.5% of revenue for 2016.

Revenue Categories used by Management

In addition to the line item revenue categories discussed above, management also uses revenue categorizations which breakdown revenue into other groupings. Management regularly disaggregates revenue in the following categories, which it finds relevant and useful:

- Ion implant revenue separate from revenue from legacy non-implant product lines, given that ion implantation systems are critical to our growth and strategic objectives;
- Systems and aftermarket revenues, in which “Aftermarkets” is
 - A. the portion of Product revenue relating to spare parts, product upgrades and used systems combined with
 - B. Service revenue, which is the labor component of aftermarket revenues;

Aftermarket purchases reflect current fab utilization as opposed to System purchases which reflect capital investment decisions by our customers, which have differing economic drivers;

- Revenue by geographic regions, since economic factors impacting customer purchasing decisions may vary by geographic region; and
- Revenue by our customers’ end markets, since they tend to be subject to different economic environments at different periods of time, impacting a customer’s likelihood of purchasing capital equipment during any particular period; currently, management uses three end market categories: Memory, mature technology processes and leading edge foundry and logic.

The ion implant and aftermarket revenue categories for recent periods are discussed below.

2018 Compared with 2017

Ion Implant

Revenue from sales of ion implantation products and related service was \$421.7 million, or 95.3% of total revenue in 2018, compared with \$391.1 million, or 95.2%, of total revenue in 2017.

Aftermarket

We refer to the business of selling spare parts, product upgrades, and used systems, combined with the sale of maintenance labor and service contracts and service hours, as the “aftermarket” business. Revenue from our aftermarket business was \$162.2 million in 2018, compared to \$147.9 million for 2017. Aftermarket revenue generally increases with the expansion of the installed base of systems but can fluctuate from period to period based on capacity utilization at customers’ manufacturing facilities which affects the sale of spare parts and demand for equipment service.

2017 Compared with 2016

Ion Implant

Revenue from sales of ion implantation products and related service was \$391.1 million, or 95.2% of total revenue in 2017, compared with \$248.9 million, or 93.2%, of total revenue in 2016.

Aftermarket

Revenue from our aftermarket business was \$147.9 million in 2017, compared to \$127.7 million for 2016.

Gross Profit / Gross Margin

The following table sets forth our gross profit:

	Year ended December 31, 2018 2017 (dollars in thousands)				Period-to-Period Change \$ %		Year ended December 31, 2017 2016				Period-to-Period Change \$ %	
Gross Profit:												
Product	\$ 179,476		\$ 152,192		\$ 27,284	17.9 %	\$ 152,192		\$ 95,288		\$ 56,904	59.7 %
Product gross margin	43.2 %		39.3 %				39.3 %		39.0 %			
Services	160		(1,945)		2,105	(108.2) %	(1,945)		\$ 4,310		(6,255)	(145.1) %
Services gross margin	0.6 %		(8.3) %				(8.3) %		19.0 %			
Total gross profit	\$ 179,636		\$ 150,247		\$ 29,389	19.6 %	\$ 150,247		\$ 99,598		\$ 50,649	50.9 %
Gross margin	40.6 %		36.6 %				36.6 %		37.3 %			

2018 Compared with 2017

Product

Gross margin from product revenue was 43.2% for the twelve months ended December 31, 2018, compared to 39.3% for the twelve months ended December 31, 2017. The increase in gross margin of 3.9% resulted from improved margins on Purion systems and a lower excess reserve for inventory due to a \$6.2 million write-down of Legacy inventory in 2017.

Services

Gross margin from services revenue was 0.6% for the twelve months ended December 31, 2018, compared to (8.3)% for the twelve months ended December 31, 2017. The increase in gross margin in the recent period is primarily attributable to decreased costs on service contracts.

2017 Compared with 2016

Product

Gross margin from product revenue was 39.3% for the twelve months ended December 31, 2017, compared to 39.0% for the twelve months ended December 31, 2016. The increase in gross margin of 0.3% resulted from improved margins on Purion systems, partially offset by a \$6.2 million write-down of Legacy inventory in 2017.

Services

Gross margin from services revenue was (8.3)% for the twelve months ended December 31, 2017, compared to 19.0% for the twelve months ended December 31, 2016. The decrease in gross margin is primarily attributable to increased costs on service contracts.

Operating Expenses

The following table sets forth our operating expenses:

	Year ended December 31, 2018 (dollars in thousands)				Period-to-Period Change		Year ended December 31, 2017				Period-to-Period Change	
					\$	%					\$	%
Research and development	\$ 51,876		\$ 43,071		\$ 8,805	20.4 %	\$ 43,071		\$ 34,402		\$ 8,669	25.2 %
Percentage of revenue	11.7	%	10.5	%			10.5	%	12.9	%		
Sales and marketing	34,608		28,532		6,076	21.3 %	28,532		23,839		4,693	19.7 %
Percentage of revenue	7.8	%	6.9	%			6.9	%	8.9	%		
General and administrative	33,193		30,802		2,391	7.8 %	30,802		24,452		6,350	26.0 %
Percentage of revenue	7.5	%	7.5	%			7.5	%	9.2	%		
Restructuring charges	—		—		—	— %	—		282		(282)	(100)%
Percentage of revenue	—	%	—	%			—	%	0.1	%		
Total operating expenses	\$ 119,677		\$ 102,405		\$ 17,272	16.9 %	\$ 102,405		\$ 82,975		\$ 19,430	23.4 %
Percentage of revenue	27.0	%	24.9	%			24.9	%	31.1%	%		

Our operating expenses consist primarily of personnel costs, including salaries, commissions, bonuses, stock-based compensation and related benefits and taxes; project material costs related to the design and development of new products and enhancement of existing products; and professional fees, travel and depreciation expenses. Personnel costs are our largest expense, representing \$74.3 million, or 62.1% of our total operating expenses, for the year ended December 31, 2018; \$64.5 million, or 63.0%, of our total operating expenses for the year ended December 31, 2017; and \$47.6 million, or 57.5%, of our total operating expenses for the year ended December 31, 2016.

Research and Development

Year ended	Period-to-Period	Year ended	Period-to-Period
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	December 31, 2018				Change		December 31, 2017				Change		
	2017				\$	%	2016				\$	%	
	(dollars in thousands)												
Research and development	\$	51,876	\$	43,071	\$	8,805	20.4	\$	43,071	\$	34,402	8,669	25.2
Percentage of revenue		11.7	%	10.5	%				10.5	%	12.9	%	

Our ability to remain competitive depends largely on continuously developing innovative technology, with new and enhanced features and systems and introducing them at competitive prices on a timely basis. Accordingly, based on our strategic plan, we establish annual R&D budgets to fund programs that we expect will drive competitive advantages.

2018 Compared with 2017

Research and development expense was \$51.9 million in 2018, an increase of \$8.8 million, or 20.4%, compared with \$43.1 million in 2017. The increase was primarily due to increased headcount and to project costs to support development of new Purion products and extensions.

2017 Compared with 2016

Research and development expense was \$43.1 million in 2017, an increase of approximately \$8.7 million, or 25.2%, compared with \$34.4 million in 2016. The increase was primarily due to variable incentive plan expense and to a lesser extent to increased headcount.

Sales and Marketing

	Year ended December 31,		Period-to-Period Change		Year ended December 31,		Period-to-Period Change	
	2018	2017	\$	%	2017	2016	\$	%
	(dollars in thousands)							
Sales and marketing	\$ 34,608	\$ 28,532	\$ 6,076	21.3 %	\$ 28,532	\$ 23,839	\$ 4,693	19.7 %
Percentage of revenue	7.8 %	6.9 %			6.9 %	8.9 %		

Our sales and marketing expenses result primarily from the sale of our equipment and services through our direct sales force.

2018 Compared with 2017

Sales and marketing expense was \$34.6 million in 2018, an increase of \$6.1 million, or 21.3%, compared with \$28.5 million in 2017. The increase was primarily due to increased headcount.

2017 Compared with 2016

Sales and marketing expense was \$28.5 million in 2017, an increase of \$4.7 million, or 19.7%, compared with \$23.8 million in 2016. The increase was primarily due to variable incentive plan expense and to a lesser extent to increased headcount.

General and Administrative

	Year ended December 31,		Period-to-Period Change		Year ended December 31,		Period-to-Period Change	
	2018	2017	\$	%	2017	2016	\$	%
	(dollars in thousands)							
	\$ 33,193	\$ 30,802	\$ 2,391	7.8 %	\$ 30,802	\$ 24,452	6,350	26.0 %

General and
administrative
Percentage of
revenue

7.5	%	7.5	%	7.5	%	9.2	%
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Our general and administrative expenses result primarily from the costs associated with our executive, finance, information technology, legal and human resource functions.

2018 Compared with 2017

General and administrative expense was \$33.2 million in 2018, an increase of \$2.4 million, or 7.8% compared with \$30.8 million in 2017. The increase was primarily due to increases in professional and consulting fees and to a lesser extent, increased headcount.

2017 Compared with 2016

General and administrative expense was \$30.8 million in 2017, an increase of \$6.4 million, or 26.0% compared with \$24.5 million in 2016. The increase was primarily due to variable incentive plan expense and to a lesser extent to increased headcount.

Restructuring

We from time to time incur expenses relating to restructuring.

2017 Compared with 2016

During the year ended December 31, 2016 we recorded \$0.3 million to restructuring expense due to a consolidation in our customer base.

Other (Expense) Income

Other (expense) income consists primarily of interest expense relating to the lease obligation we incurred in connection with the 2015 sale of our headquarters facility (“sale leaseback”) and other financing obligations, foreign exchange gains and losses attributable to fluctuations of the U.S. dollar against the local currencies of certain of the countries in which we operate, as well as interest earned on our invested cash balances.

	Year ended December 31,		Period-to-Period Change		Year ended December 31,		Period-to-Period Change	
	2018	2017	\$	%	2017	2016	\$	%
(dollars in thousands)								
Other expense	\$ (5,254)	\$ (4,011)	\$ (1,243)	31 %	\$ (4,011)	\$ (5,599)	1,588	(28.4) %
Percentage of revenue	(1.3) %	(1.0) %			(1.0) %	(2.1) %		

2018 Compared with 2017

Other expense for the year ended December 31, 2018 was \$5.3 million, which includes \$5.1 million of interest expense related to our sale leaseback obligation, \$1.3 million of foreign currency translation losses, other miscellaneous expense of \$1.2 million, partially offset by interest income of \$2.3 million. Other expense for the year ended December 31, 2017 was \$4.0 million, which includes \$5.1 million of interest expense related to our sale leaseback obligation and other miscellaneous expense of \$0.7 million, partially offset by interest income of \$0.7 million and \$1.1 million of foreign currency translation gains.

2017 Compared with 2016

Other expense for the year ended December 31, 2017 was \$4.0 million, which includes \$5.1 million of interest expense related to our sale leaseback obligation and other miscellaneous expense of \$0.7 million, offset by interest income of \$0.7 million and \$1.1 million of foreign currency translation gains. Other expense for the year ended December 31, 2016 was \$5.6 million and includes interest expense of \$5.1 million, interest income of \$0.2 million and \$0.6 million of foreign currency translation loss.

Income Taxes

	Year ended December 31, 2018 2017		Period-to-Period Change		Year ended December 31, 2017 2016		Period-to-Period Change	
	(dollars in thousands)		\$	%			\$	%
Income tax provision (benefit)	\$ 8,820	\$ (83,128)	\$ 91,948	(111) %	\$ (83,128)	\$ 23	(83,151)	*NM %
Percentage of revenue	1.9 %	(20.2) %			(20.2) %	— %		

2018 Compared with 2017

Income tax expense was \$8.8 million for the year ended December 31, 2018 compared to an income tax benefit of \$83.1 million in the previous year. The income tax expense of \$8.8 million in 2018 reflects a net effective tax rate of 16.1% on our worldwide pre-tax income. The income tax benefit of \$83.1 million in 2017 was primarily due to the release of our valuation allowance on our deferred tax assets. We have significant net operating loss carryforwards in the United States and certain European jurisdictions, and, as a result, we do not currently pay significant income taxes in those jurisdictions.

At December 31, 2018, we had \$71.9 million of deferred tax assets worldwide relating to net operating loss carryforwards, tax credit carryforwards and other temporary differences, which are available to reduce income taxes in future years. We have continued to maintain a \$6.8 million valuation allowance in the U.S. against certain tax credits and state net operating losses due to the uncertainty of their realization based on long-term Company forecasts and the expiration dates on these attributes. If future operating results of the U.S. or these foreign jurisdictions significantly exceed expectations, it is reasonably possible that there could be a further reduction in the valuation allowance in the future. Further reduction of the valuation allowance, in whole or in part, would result in a non-cash income tax benefit during the period of reduction.

2017 Compared with 2016

Income tax benefit was \$83.1 million for the year ended December 31, 2017, compared to \$0.1 million income tax expense for the year ended December 31, 2016. The income tax benefit of \$83.1 million in 2017 was primarily due to the release of our valuation allowance on our deferred tax assets. Our income tax expense for the year ended December 31, 2016 was due to operating results of foreign entities in jurisdictions in Europe and Asia, where we earned taxable income.

Liquidity and Capital Resources

Our liquidity is affected by many factors. Some of these relate specifically to the operations of our business. For example, our sales and other factors relate to the uncertainties of global economies, including the availability of credit and the condition of the overall semiconductor capital equipment industry. Our established cost structure does not vary significantly with changes in volume. We experience fluctuations in operating results and cash flows depending on fluctuations in our revenue level.

In 2018, \$47.0 million of cash was provided by operating activities. This compares to \$56.3 million of cash provided by operations in 2017. Cash and cash equivalents at December 31, 2018 was \$178.0 million, compared to \$133.4 million at December 31, 2017. Approximately \$16.2 million of cash was located in foreign jurisdictions as of

December 31, 2018. In addition to the cash and cash equivalent balance at December 31, 2018, we had \$6.9 million in restricted cash which relates to a \$5.9 million letter of credit associated with the security deposit for the lease on our corporate headquarters in Beverly, Massachusetts, a \$0.8 million letter of credit relating to workers' compensation insurance, a \$0.1 million bank guarantee and a \$0.1 million deposit relating to customs activity. Working capital at December 31, 2018 was \$311.8 million. At December 31, 2018, we had no bank debt.

Capital expenditures were \$4.7 million and \$7.3 million for the years ended December 31, 2018 and 2017, respectively. Total capital expenditures for 2019 are projected to be approximately \$14.5 million. Future capital expenditures beyond 2019 will depend on a number of factors, including the timing and rate of expansion of our business and our ability to generate cash to fund them.

Cash provided by financing activities was \$1.2 million and \$15.1 million for the years ended December 31, 2018 and 2017, respectively. In both years, the cash provided by financing activities was mainly due to the exercise of stock options and proceeds received from the employee stock purchase plan.

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We have outstanding letters of credit and surety bonds in the amount of \$10.7 million to cover the security deposit under the lease of our headquarters, workers' compensation insurance program, customs and bank deposits and certain value added tax claims in Europe.

On January 12, 2019 we announced that our Board of Directors authorized a one-year share repurchase program of up to \$35 million of our common stock. These shares may be purchased in the open market or through privately negotiated transactions. We have no obligation to repurchase shares under the authorization, and the timing, actual number and value of shares which are repurchased will depend on a number of factors, including the price of our common stock, general business and market conditions, and alternative investment opportunities. We may suspend or discontinue the repurchase program at any time.

The following represents our commercial commitments as of December 31, 2018 (in thousands):

Other Commercial Commitments	Total	Amount of Commitment Expiration by Period		
		2019	2020	2021
Surety bonds	\$ 4,066	\$ 1,167	\$ 287	\$ 2,612
Standby letters of credit, deposits and bank guarantees	6,864	6,799	65	—
Total	\$ 10,930	\$ 7,966	\$ 352	\$ 2,612

The following represents our contractual obligations as of December 31, 2018 (in thousands):

Contractual Obligations	Total	Payments Due by Period			
		2019	2020-2021	2022-2023	2024 - Beyond
Sale leaseback obligation	\$ 115,161	\$ 5,594	\$ 11,568	\$ 12,094	\$ 85,905
Purchase order commitments	61,573	60,342	208	1,023	—
Operating leases	6,096	3,244	2,741	110	1
Total	\$ 182,830	\$ 69,180	\$ 14,517	\$ 13,227	\$ 85,906

We have no off balance sheet arrangements at December 31, 2018, exclusive of operating leases.

We have net operating loss and tax credit carryforwards, the tax effect of which aggregate \$67.1 million at December 31, 2018. These carryforwards, which expire principally between 2019 and 2038, are available to reduce future income tax liabilities in the United States and certain foreign jurisdictions.

We consider the undistributed earnings of our foreign subsidiaries as of December 31, 2018, to be indefinitely reinvested and, accordingly, no U.S. income taxes have been provided thereon. As of December 31, 2018, the amount of cash associated with indefinitely reinvested foreign earnings was approximately \$4.9 million. We have not, nor do we anticipate the need to, repatriate funds to the United States to satisfy domestic liquidity needs arising in the ordinary course of business, including liquidity needs associated with our domestic debt service requirements. We anticipate that U.S. tax resulting from remitting such earnings will be off set by net operating loss or credit carryforwards to the extent available. In addition, we do not anticipate incurring a foreign withholding tax on remitting such earnings since we do not intend to remit the earnings as dividends.

We believe that based on our current market, revenue, expense and cash flow forecasts, our existing cash, cash equivalents and borrowing capacity will be sufficient to satisfy our anticipated cash requirements for the short and long term. We currently have no credit facility but management believes we would be able to borrow on reasonable terms if needed.

Related Party Transactions

There are no significant related party transactions that require disclosure in the consolidated financial statements for the year ended December 31, 2018, or in this Annual Report on Form 10-K.

Recent Accounting Pronouncements

A discussion of recent accounting pronouncements, the impact of some of which may be material, is included in Note 2 to the consolidated financial statements for the year ended December 31, 2018 included in this Annual Report on Form 10-K.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

Interest Rate Sensitivity

Our exposure to market risk for changes in interest rates relates primarily to our investment portfolio, which consists entirely of cash equivalents at December 31, 2018. The primary objective of our investment activities is to preserve principal. This is accomplished by investing in marketable investment grade securities. We do not use derivative financial instruments in managing our investment portfolio. Due to the nature of our investments, we do not expect our operating results or cash flows to be affected to any significant degree by any change in market interest rates.

Foreign Currency Exchange Risk

Substantially all of our sales are billed in U.S. dollars, thereby reducing the impact of fluctuations in foreign exchange rates on our results. Operating margins of certain foreign operations can fluctuate with changes in foreign exchange rates to the extent revenue is billed in U.S. dollars and operating expenses are incurred in the local currency. During the years ended December 31, 2018 and 2017, approximately 22.5% and 23.5% of our revenue were derived in local currencies from foreign operations with this inherent risk. In addition, at both December 31, 2018 and 2017, our operations outside of the United States accounted for approximately 12.9% and 14.6% of our total assets, respectively, the majority of which was denominated in currencies other than the U.S. dollar. We do not use derivative financial instruments in managing our foreign currency exchange risk.

Item 8. Financial Statements and Supplementary Data.

Response to this Item is submitted as a separate section of this report immediately following Item 15.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

Item 9A. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures.

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) as of the end of the period covered by this annual report (the “Evaluation Date”). Based on this evaluation, our principal executive officer and principal financial officer concluded that, as of the Evaluation Date, these disclosure controls and procedures are effective.

Internal Control over Financial Reporting

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Exchange Act. Because of its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements. A control system, no matter how well designed and operated, can provide only reasonable assurance with respect to financial statement preparation and presentation. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2018. In making this assessment, management used the criteria set forth in the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control—2013 Integrated Framework.

Based on this assessment, management has concluded that, as of December 31, 2018, our internal control over financial reporting is effective based on those criteria.

The independent registered public accounting firm of Ernst & Young LLP, as auditors of our consolidated financial statements, has issued an attestation report on its assessment of our internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

To the Stockholders and the Board of Directors of Axcelis Technologies, Inc.

Opinion on Internal Control over Financial Reporting

We have audited Axcelis Technologies, Inc.'s internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, Axcelis Technologies, Inc. (the Company) maintained, in all material respects, effective internal controls over financial reporting as of December 31, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the 2018 consolidated financial statements of the Company and our report dated March 11, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Ernst & Young LLP

Boston, Massachusetts

March 11, 2019

32

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) identified in connection with the evaluation of our internal control that occurred during our fourth quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

A portion of the information required by Item 10 of Form 10 K is incorporated by reference from the information responsive thereto contained in the sections in Axcelis Proxy Statement for the Annual Meeting of Stockholders to be held May 14, 2019 (the “Proxy Statement”) captioned:

- “Proposal 1: Election of Directors,”
- “Board of Directors,”
- “Board Committees,” and
- “Corporate Governance,”

The remainder of such information is set forth under the heading “Executive Officers of the Registrant” at the end of Item 1 in Part I of this report and is incorporated herein by reference.

Item 11. Executive Compensation.

The information required by Item 11 of Form 10 K is incorporated by reference from the information responsive thereto contained in the sections in the Proxy Statement captioned:

- “Executive Compensation,” and
- “Board Committees—Compensation Committee Interlocks and Insider Participation.”

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information required by Item 12 of Form 10 K is incorporated by reference from the information responsive thereto contained in the sections in the Proxy Statement captioned:

- “Share Ownership of 5% Stockholders,” and
- “Share Ownership of Directors and Executive Officers,”

Item 13. Certain Relationships and Related Transactions and Director Independence.

The information required by Item 13 of Form 10 K is incorporated by reference from the information responsive thereto contained in the sections in the Proxy Statement captioned:

- “Executive Compensation,”
- “Board of Directors,” and
- “Corporate Governance—Certain Relationships and Related Transactions.”

Item 14. Principal Accounting Fees and Services

The information required by Item 14 of Form 10 K is incorporated by reference from the information responsive thereto contained in the section captioned “Proposal 3: Ratification of the Appointment of our Independent Registered Public Accounting Firm” in the Proxy Statement.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a)The following documents are filed as part of this Report:

1) Financial Statements:

<u>Report of Independent Registered Public Accounting Firm</u>	36
<u>Consolidated Statements of Operations — For the years ended December 31, 2018, 2017 and 2016</u>	37
<u>Consolidated Statements of Comprehensive Income — For the years ended December 31, 2018, 2017 and 2016</u>	38
<u>Consolidated Balance Sheets — December 31, 2018 and 2017</u>	39
<u>Consolidated Statements of Stockholders' Equity — For the years ended December 31, 2018, 2017 and 2016</u>	40
<u>Consolidated Statements of Cash Flows — For the years ended December 31, 2018, 2017 and 2016</u>	41
<u>Notes to Consolidated Financial Statements</u>	42

2) Exhibits

The exhibits filed as part of this Form 10 K are listed on the Exhibit Index immediately preceding the signature page, which Exhibit Index is incorporated herein by reference.

3) Financial Statement Schedules:

Schedule II—Valuation and Qualifying Accounts for the years ended December 31, 2018, 2017 and 2016.

All other schedules for which provision is made in the applicable regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable, and therefore have been omitted.

Item 16. Form 10-K Summary

Not applicable.

35

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and the Board of Directors of Axcelis Technologies, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Axcelis Technologies, Inc. (the Company) as of December 31, 2018 and 2017, the related consolidated statements of operations, comprehensive income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2018, and the related notes and financial statement schedule listed in the Index at Item 15(a), collectively referred to as the "consolidated financial statements". In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 11, 2019 expressed an unqualified opinion thereon.

Adoption of New Accounting Standard

As discussed in Note 2 to the consolidated financial statements, the Company changed its method for accounting for revenue in 2018.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Ernst & Young LLP

We have served as the Company's auditor since 1999.

Boston, Massachusetts

March 11, 2019

Axcelis Technologies, Inc.

Consolidated Statements of Operations

(In thousands, except per share amounts)

	Twelve months ended December 31,		
	2018	2017	2016
Revenue:			
Product	\$ 415,922	\$ 387,124	\$ 244,295
Services	26,653	23,437	22,685
Total revenue	442,575	410,561	266,980
Cost of revenue:			
Product	236,446	234,932	149,007
Services	26,493	25,382	18,375
Total cost of revenue	262,939	260,314	167,382
Gross profit	179,636	150,247	99,598
Operating expenses:			
Research and development	51,876	43,071	34,402
Sales and marketing	34,608	28,532	23,839
General and administrative	33,193	30,802	24,452
Restructuring charges	—	—	282
Total operating expenses	119,677	102,405	82,975
Income from operations	59,959	47,842	16,623
Other (expense) income:			
Interest income	2,328	714	238
Interest expense	(5,110)	(5,121)	(5,073)
Other, net	(2,472)	396	(764)
Total other expense	(5,254)	(4,011)	(5,599)
Income before income taxes	54,705	43,831	11,024
Income tax provision (benefit)	8,820	(83,128)	23
Net income	\$ 45,885	\$ 126,959	\$ 11,001
Net income per share:			
Basic	\$ 1.42	\$ 4.11	\$ 0.38
Diluted	\$ 1.35	\$ 3.80	\$ 0.36
Shares used in computing net income per share:			
Basic weighted average common shares	32,286	30,866	29,195
Diluted weighted average common shares	34,002	33,436	30,947

See accompanying Notes to these Consolidated Financial Statements

Axcelis Technologies, Inc.

Consolidated Statements of Comprehensive Income

(In thousands)

	Twelve months ended December 31,		
	2018	2017	2016
Net income	\$ 45,885	\$ 126,959	\$ 11,001
Other comprehensive (loss) income:			
Foreign currency translation adjustments	(1,794)	4,347	(847)
Amortization of actuarial loss and other adjustments from pension plan	66	108	(1)
Total other comprehensive (loss) income	(1,728)	4,455	(848)
Comprehensive income	\$ 44,157	\$ 131,414	\$ 10,153

See accompanying Notes to these Consolidated Financial Statements

Axcelis Technologies, Inc.

Consolidated Balance Sheets

(In thousands, except per share amounts)

	December 31, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 177,993	\$ 133,407
Short-term restricted cash	—	750
Accounts receivable, net	78,727	75,302
Inventories, net	129,000	120,544
Prepaid expenses and other current assets	11,051	9,772
Total current assets	396,771	339,775
Property, plant and equipment, net	41,149	36,168
Long-term restricted cash	6,909	6,723
Deferred income taxes	71,939	83,148
Other assets	31,673	22,404
Total assets	\$ 548,441	\$ 488,218
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 35,955	\$ 32,642
Accrued compensation	19,218	20,955
Warranty	4,819	4,112
Income taxes	462	273
Deferred revenue	19,513	16,181
Other current liabilities	5,030	5,124
Total current liabilities	84,997	79,287
Sale leaseback obligation	47,757	47,714
Long-term deferred revenue	3,071	1,964
Other long-term liabilities	4,279	5,643
Total liabilities	140,104	134,608
Commitments and contingencies (Note 16)		
Stockholders' equity:		
Common stock, \$0.001 par value, 75,000 shares authorized; 32,558 shares issued and outstanding at December 31, 2018; 32,048 shares issued and outstanding at December 31, 2017	33	32
Additional paid-in capital	565,116	556,147
Accumulated deficit	(157,260)	(204,745)
Accumulated other comprehensive income	448	2,176
Total stockholders' equity	408,337	353,610
Total liabilities and stockholders' equity	\$ 548,441	\$ 488,218

See accompanying Notes to these Consolidated Financial Statements

Axcelis Technologies, Inc.

Consolidated Statements of Stockholders' Equity

(In thousands)

	Common Shares	Stock Amount	Additional Paid-in Capital	Treasury Stock	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance at December 31, 2015	29,026	\$ 29	\$ 529,089	\$ (1,218)	\$ (342,705)	\$ (1,431)	\$ 183,764
Net income	—	—	—	—	11,001	—	11,001
Foreign currency translation adjustments	—	—	—	—	—	(847)	(847)
Change in pension obligation	—	—	—	—	—	(1)	(1)
Exercise of stock options	392	1	2,237	—	—	—	2,238
Issuance of shares under Employee Stock Purchase Plan	22	—	325	—	—	—	325
Issuance of restricted common shares	108	—	(11)	—	—	—	(11)
Treasury shares returned to authorized	(30)	—	(1,218)	1,218	—	—	—
Reverse stock split issuance costs	—	—	(145)	—	—	—	(145)
Stock-based compensation expense	—	—	5,131	—	—	—	5,131
Balance at December 31, 2016	29,518	30	535,408	—	(331,704)	(2,279)	201,455
Net income	—	—	—	—	126,959	—	126,959
Foreign currency	—	—	—	—	—	4,347	4,347

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translation adjustments							
Change in pension obligation	—	—	—	—	—	108	108
Exercise of stock options	2,358	2	15,512	—	—	—	15,514
Issuance of shares under Employee Stock Purchase Plan	34	—	845	—	—	—	845
Issuance of restricted common shares	138	—	(1,164)	—	—	—	(1,164)
Stock-based compensation expense	—	—	5,546	—	—	—	5,546
Balance at December 31, 2017	32,048	32	556,147	—	(204,745)	2,176	353,610
Net income	—	—	—	—	45,885	—	45,885
Foreign currency translation adjustments	—	—	—	—	—	(1,794)	(1,794)
Change in pension obligation	—	—	—	—	—	66	66
Exercise of stock options	273	1	1,733	—	—	—	1,734
Issuance of shares under Employee Stock Purchase Plan	55	—	1,025	—	—	—	1,025
Issuance of restricted common shares	182	—	(1,419)	—	—	—	(1,419)
Adjustment to Retained Earnings upon ASC 606 Adoption	—	—	—	—	1,600	—	1,600
Stock-based compensation expense	—	—	7,630	—	—	—	7,630
Balance at December 31, 2018	32,558	\$ 33	\$ 565,116	\$ —	\$ (157,260)	\$ 448	\$ 408,337

See accompanying Notes to these Consolidated Financial Statements

Axcelis Technologies, Inc.

Consolidated Statements of Cash Flows

(In thousands)

	Twelve months ended December 31,		
	2018	2017	2016
Cash flows from operating activities			
Net income	\$ 45,885	\$ 126,959	\$ 11,001
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation and amortization	5,772	5,002	4,258
Gain on sale of equipment	—	—	(248)
Deferred income taxes	11,209	(82,085)	519
Stock-based compensation expense	7,784	5,672	5,179
Provision for doubtful accounts	—	—	106
Provision for excess and obsolete inventory	2,205	8,135	1,051
Changes in operating assets & liabilities:			
Accounts receivable	(3,877)	(23,573)	(14,135)
Inventories	(10,512)	(10,567)	(6,572)
Prepaid expenses and other current assets	(1,436)	(3,866)	(1,056)
Accounts payable and other current liabilities	(703)	25,000	810
Deferred revenue	6,055	7,079	2,467
Income taxes	196	14	102
Other assets and liabilities	(15,613)	(1,486)	(12,270)
Net cash provided by (used in) operating activities	46,965	56,284	(8,788)
Cash flows from investing activities			
Proceeds from sale of equipment	—	—	270
Expenditures for property, plant and equipment and capitalized software	(4,715)	(7,285)	(2,506)
Net cash used in investing activities	(4,715)	(7,285)	(2,236)
Cash flows from financing activities			
Net settlement on restricted stock grants	(1,419)	(1,184)	(11)
Financing fees and other expenses	—	—	(146)
Proceeds from Employee Stock Purchase Plan	871	739	277
Proceeds from exercise of stock options	1,734	15,515	2,227
Net cash provided by financing activities	1,186	15,070	2,347
Effect of exchange rate changes on cash and cash equivalents	586	(844)	507
Net increase (decrease) in cash, cash equivalents and restricted cash	44,022	63,225	(8,170)
Cash, cash equivalents and restricted cash at beginning of period	140,880	77,655	85,825

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Cash, cash equivalents and restricted cash at end of period	\$ 184,902	\$ 140,880	\$ 77,655
Supplemental disclosure of cash flow information			
Cash paid for:			
Income taxes	\$ 858	\$ 583	\$ 525
Interest	\$ 5,470	\$ 5,315	\$ 4,815

See accompanying Notes to these Consolidated Financial Statements

Axcelis Technologies, Inc.

Notes to Consolidated Financial Statements

Note 1. Nature of Business

Axcelis Technologies, Inc. (“Axcelis” or the “Company”) was incorporated in Delaware in 1995, and is a worldwide producer of ion implantation and other processing equipment used in the fabrication of semiconductor chips in the United States, Europe and Asia. In addition, we provide extensive aftermarket service and support, including spare parts, equipment upgrades, used equipment and maintenance services to the semiconductor industry.

Note 2. Summary of Significant Accounting Policies

The accompanying consolidated financial statements reflect the application of certain significant accounting policies as described in this note and elsewhere in the footnotes.

(a) Basis of Presentation

The accompanying consolidated financial statements include the consolidated accounts of the Company and its wholly owned, controlled subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Events occurring subsequent to December 31, 2018 have been evaluated for potential recognition or disclosure in the consolidated financial statements.

(b) Use of Estimates

The preparation of these consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. On an ongoing basis, we evaluate our estimates and judgments, including those related to revenue recognition, the realizable value of inventories, valuing stock-based compensation instruments and reserves relating to tax assets and liabilities. Actual

amounts could differ from these estimates. Changes in estimates are recorded in the period in which they become known.

(c) Foreign Currency

The functional currency for substantially all operations outside the United States is the local currency. Financial statements for these operations are translated into United States dollars at year end rates as to assets and liabilities and average exchange rates during the year as to revenue and expenses. The resulting translation adjustments are recorded in stockholders' equity as an element of accumulated other comprehensive income (loss). Foreign currency transaction gains and losses are included in other income (expense) in the Consolidated Statements of Operations.

For the year ended December 31, 2018 we had \$1.3 million in foreign exchange loss. For the year ended December 31, 2017 we had \$1.1 million in foreign exchange gains. For the year ended December 31, 2016 we had \$0.6 million in foreign exchange losses.

(d) Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand and highly liquid investments with original maturities of ninety days or less. Cash equivalents consist primarily of money market funds, U.S Government and Agency Securities and deposit accounts. Cash equivalents are carried on the balance sheet at fair market value.

(e) Inventories

Inventories are carried at lower of cost or net realizable value, determined using the first in, first out (“FIFO”) method, or market. We periodically review our inventories and make provisions as necessary for estimated obsolescence or damaged goods to ensure values approximate lower of cost or net realizable value. The amount of such markdowns is equal to the difference between cost of inventory and the estimated market value based upon assumptions about future demands, selling prices, and market conditions.

We record a provision for estimated excess inventory. The provision is determined using management’s assumptions of materials usage, based on estimates of demand and market conditions. If actual market conditions become less favorable than those projected by management, additional inventory write downs may be required.

(f) Property, Plant and Equipment

Property, plant and equipment are stated at cost, less accumulated depreciation and amortization.

Depreciation and amortization are recorded using the straight line method over the estimated useful lives of the related assets as follows:

Asset Classification	Estimated Useful Life
Land and buildings (under lease)	Lesser of the lease term or estimated useful life of the asset
Machinery and equipment	7 to 10 years

On January 30, 2015, we sold our corporate headquarters facility. As part of this sale, we also entered into a 22-year lease agreement. We accounted for the sale leaseback transaction as a financing arrangement for financial reporting purposes. We retained the historical costs of the property and the related accumulated depreciation on our financial books within property, plant and equipment and will continue to depreciate the property for financial reporting purposes over the lesser of its remaining useful life or its initial lease term of 22 years.

Repairs and maintenance costs are expensed as incurred. Expenditures for renewals and betterments are capitalized.

(g) Impairment of Long Lived Assets

We record impairment losses on long-lived assets when events and circumstances indicate that these assets might not be recoverable. Recoverability is measured by a comparison of the assets' carrying amount to their expected future undiscounted net cash flows. If such assets are considered to be impaired, the impairment is measured based on the amount by which the carrying value exceeds its fair value.

We did not have any indicators of impairment during the period ending December 31, 2018. We did not record an impairment charge in the years ended December 31, 2018, 2017, or 2016.

Actual performance could be materially different from our current forecasts, which could impact estimates of undiscounted cash flows and may result in the impairment of the carrying amount of the long-lived assets in the future. This could be caused by strategic decisions made in response to economic and competitive conditions, the impact of the economic environment on our customer base, or a material adverse change in our relationships with significant customers.

(h) Concentration of Risk and Off Balance Sheet Risk

Financial instruments that potentially subject us to concentrations of credit risk are principally cash equivalents and accounts receivable. Our cash equivalents are principally maintained in investment grade money market funds, U.S. Government and Agency Securities and deposit accounts.

We have no significant off balance sheet risk such as currency exchange contracts, option contracts or other hedging arrangements.

Our exposure to market risk for changes in interest rates relates primarily to cash equivalents. The primary objective of our investment activities is to preserve principal without significantly increasing risk. This is accomplished by investing in marketable investment grade securities. We do not use derivative financial instruments to manage our investment portfolio and do not expect operating results or cash flows to be affected to any significant degree by any change in market interest rates.

We perform ongoing credit evaluations of our customers' financial condition and generally requires no collateral to secure accounts receivable. For selected overseas sales, we require customers to obtain letters of credit before product is shipped. We maintain an allowance for doubtful accounts based on our assessment of the collectability of accounts receivable. We review the allowance for doubtful accounts quarterly. We do not have any off balance sheet credit exposure related to our customers.

Our customers consist of semiconductor chip manufacturers located throughout the world and net sales to our ten largest customers accounted for 76.9%, 73.3% and 70.2% of revenue in 2018, 2017 and 2016, respectively.

For the year ended December 31, 2018, we had two customers representing 20.1% and 12.1% of total revenue, respectively. For the year ended December 31, 2017 we had two customers representing 24.9% and 13.1% of total revenue, respectively. For the year ended December 31, 2016, we had one customer representing 17.0% of total revenue.

As of December 31, 2018, we had two customers account for 21.9% and 11.5% of consolidated accounts receivable, respectively. As of December 31, 2017, we had three customers account for 19.8%, 11.8% and 10.6% of consolidated accounts receivable, respectively.

Some of the components and sub assemblies included in our products are obtained either from a sole source or a limited group of suppliers. Disruption to our supply source, resulting either from economic conditions or other factors,

could affect our ability to deliver products to our customers.

(i) Revenue Recognition

Under Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 606, Revenue from Contracts with Customers or (“ASC 606”), revenue is recognized when a customer obtains control of promised goods or services in an amount that reflects the consideration we expect to receive in exchange for those goods or services. We measure revenue based on the consideration specified in the customer arrangement, and revenue is recognized when the performance obligations in the customer arrangement are satisfied. A performance obligation is a promise in a contract to transfer a distinct product or service to the customer. The transaction price of a contract is allocated to each distinct performance obligation based upon the relative standalone selling price for each performance obligation and recognized as revenue when or as, the customer receives the benefit of the performance obligation. To account for and measure revenue, we apply the following five steps:

1) Identify the contract with the customer

A contract with a customer exists when (i) we enter into an enforceable contract with a customer that defines each party’s rights regarding the goods or services to be transferred and identifies the related payment terms, (ii) the contract has commercial substance, and (iii) we determine that collection of substantially all consideration for goods and services that are transferred is probable based on the customer’s intent and ability to pay the promised consideration.

2) Identify the performance obligations in the contract

Performance obligations promised in a contract are identified based on the goods and services that will be transferred to the customer that are both capable of being distinct, whereby the customer can benefit from the good or service either on its own or together with other available resources, and are distinct in the context of the contract, whereby the transfer of the good or service is separately identifiable from other promises in the contract. To the extent a contract includes multiple promised goods and services, we must apply judgment to determine whether promised goods and services are capable of being distinct and distinct in the context of the contract. If these criteria are not met, the promised goods and services are accounted for as a combined performance obligation.

Systems sales consist of multiple performance obligations, including the system itself and obligations that are not delivered simultaneously with the system. These undelivered obligations might include a combination of installation services, extended warranty and support and spare parts, all of which are generally covered by a single sales price.

The aftermarket business includes both products and services type arrangements. Performance obligations in these contracts consist of used tools, spare parts, equipment upgrades, maintenance services and customer training.

Customers who purchase new systems are provided an assurance-type warranty for one year after acceptance of the tool. For aftermarket transactions, we provide customers an assurance-type warranty for 90 days. Customers can choose to purchase extended warranty terms with enhanced support similar to a service-type warranty ranging from one to three years. In accordance with ASC 606, assurance-type warranties are not considered a performance obligation, whereas service-type warranties are.

3) Determine the transaction price

The transaction price is determined based on the consideration to which we will be entitled in exchange for transferring goods and services to the customer. To the extent the transaction price includes variable consideration, we estimate the amount of variable consideration that should be included in the transaction price utilizing either the expected value method or the most likely amount method depending on the nature of the variable consideration. Variable consideration is included in the transaction price if, in our judgment, it is probable that a significant future reversal of cumulative revenue under the contract will not occur. Any estimates, including the effect of the constraint on variable consideration, are evaluated at each reporting period for any changes. In applying this guidance, Companies must also consider whether any significant financing components exist.

The transaction price for all transactions is based on the price reflected in the individual customer's purchase order. Variable consideration has not been identified as a significant component of the transaction price for any of our transactions.

For those transactions where all performance obligations will be satisfied within one year or less, we apply the practical expedient outlined in ASC 606-10-32-18. This practical expedient allows us not to adjust promised consideration for the effects of a significant financing component if we expect at contract inception that the period between when we transfer the promised good or service to a customer and when the customer pays for that good or service will be one year or less. For those transactions that are expected to be completed after one year, we have assessed that there are no significant financing components because any difference between the promised consideration and the cash selling price of the good or service is for reasons other than the provision of financing.

4) Allocate the transaction price to performance obligations in the contract

If the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. Contracts that contain multiple performance obligations require an allocation of the transaction price to each performance obligation on a relative standalone selling price basis unless the transaction price is variable and meets the criteria to be allocated entirely to a performance obligation or to a distinct service that forms part of a single performance obligation.

Where required, we determine standalone selling price (SSP) for each obligation based on consideration of both

market and Company specific factors, including the selling price and profit margin for similar products, the cost to produce, and the anticipated margin.

For those contracts that contain multiple performance obligations (primarily systems sales, as well as some aftermarket contracts requiring both time and material inputs), we must determine the SSP. We use a cost plus margin approach in determining the SSP for any materials related performance obligations (such as upgrades, spare parts, systems). To determine the SSP for labor related performance obligations (such as the labor component of installation), we use directly observable inputs based on the standalone sale prices for these services.

5) Recognize revenue when or as we have satisfied a performance obligation

We satisfy performance obligations either over time or at a point in time. Revenue is recognized over time if either 1) the customer simultaneously receives and consumes the benefits provided by the entity's performance, 2) the entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced, or 3) the entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date. If the entity does not satisfy a performance obligation over time, the related performance obligation is satisfied at a point in time by transferring the control of a promised good or service to a customer. Examples of control are using the asset to produce goods or services, enhance the value of other assets or settle liabilities, and holding or selling the asset. For over time recognition, ASC 606 requires us to select a single revenue recognition method for the performance obligation that faithfully depicts our performance in transferring control of the goods and services. The guidance allows entities to choose between two methods to measure progress toward complete satisfaction of a performance obligation:

Output methods - recognize revenue on the basis of direct measurements of the value to the customer of the goods or services transferred to date relative to the remaining goods or services promised under the contract (e.g. surveys of performance completed to date, appraisals of results achieved, milestones reached, time elapsed, and units produced or units delivered); and

Input methods - recognize revenue on the basis of the entity's efforts or inputs to the satisfaction of a performance obligation (e.g., resources consumed, labor hours expended, costs incurred, or time elapsed) relative to the total expected inputs to the satisfaction of that performance obligation.

We have the right to consideration from a customer in an amount that corresponds directly with the value to the customer of the entity's performance completed to date (i.e. certain aftermarket contracts), as such we have elected a practical expedient to recognize revenue in the amount to which the entity has a right to invoice for such services.

Product related revenues (whether for systems or aftermarket business) are recognized at a point in time, when they are shipped or delivered, depending on shipping terms.

For installation services, revenue is recognized at a point in time, once the installation of the tool is complete. The nature of the installation services are such that the customer does not simultaneously receive and consume the benefits provided by the entity's performance, nor does performance of installation services create or enhance an asset that the customer controls. Installation services do not create an asset with an alternative use to the entity, and the entity does not have an enforceable right to payment for performance completed to date.

Contract liabilities are reflected as deferred revenue on the consolidated balance sheet. Contract liabilities relate to payments invoiced or received in advance of completion of performance obligations under a contract. Contract liabilities are recognized as revenue upon the fulfillment of performance obligations.

Service-type warranties for any product are recognized over time, as these represent a stand ready obligation to service the product during the warranty period. Progress in the satisfaction of these performance obligations will be measured using an input method of time elapsed.

Maintenance and service contracts are recognized over time. Progress in the satisfaction of these performance

obligations will be measured using an input method of either time elapsed in the case of fixed period contracts, or labor hours expended, in the case of project based contracts.

(j) Recognizing Assets related to Recoverable Customer Contract Costs

We recognize an asset related to incremental costs incurred by us to obtain a contract with a customer if we expect to recover those costs. We will recognize an asset from costs incurred to fulfill a contract only if such costs relate directly to a contract with an entity that we can specifically identify, the costs incurred will generate or enhance resources that will be used in satisfying performance obligations in the future, and the costs are expected to be recovered. Any assets recognized related to costs to obtain or fulfill a contract are amortized on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the asset relates.

In substantially all of our business transactions, we incur incremental costs to obtain contracts with customers, in the form of sales commissions. We maintain a commission program which awards our employees for System sales, aftermarket activity and other individual goals. Under ASC 606, an asset is amortized on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the asset relates. However, ASC 606 provides a practical expedient to allow for the recognition of commission expense when incurred if the amortization period of the asset that the entity otherwise would have recognized is one year or less. Based on the nature of our commission agreements, all commissions are expensed as incurred based upon the expectation that the amortization period would be one year or less.

(k) Shipping and Handling Costs

Shipping and handling costs are included in cost of revenue.

(l) Stock Based Compensation

We generally recognize compensation expense for all stock-based payments to employees and directors, including grants of stock options and restricted stock units, based on the grant date fair value of those stock based payments. For stock option awards, we use the Black Scholes option pricing model, adjusted for expected forfeitures. Other valuation models may be utilized in the limited circumstances where awards with market-based vesting considerations, such as the price of our common stock, or performance based awards, are granted. Stock based compensation expense is recognized ratably over the requisite service period. For each stock option or restricted stock unit grant with vesting based on a combination of time, market or performance conditions, where vesting will occur if either condition is met, the related compensation costs are recognized over the shorter of the explicit service period or the derived service period.

See Note 13 for additional information relating to stock based compensation.

(m) Income Taxes

We record income taxes using the asset and liability method. Deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax basis, and operating loss and tax credit carryforwards.

Our consolidated financial statements contain certain deferred tax assets which have arisen primarily as a result of operating losses, as well as other temporary differences between financial and tax accounting. We establish a valuation allowance if the likelihood of realization of the deferred tax assets is reduced based on an evaluation of objective verifiable evidence. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against those net deferred tax assets. We evaluate the weight of all available evidence to determine whether it is more likely than not that some portion or all of the net deferred income tax assets will not be realized.